SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1951

No. 559

THE UNITED STATES, PETITIONER,

vs.

BELL AIRCRAFT CORPORATION.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

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1 IN THE COURT OF CLAIMS OF THE UNITED STATES

No. 47745

BELL AIRCRAFT CORPORATION, *Plaintiff*,

v.

THE UNITED STATES OF AMERICA, *Defendant*.

PETITION.

Filed July 7, 1947

To The Honorable the Chief Justice and Associate Justices of the Court of Claims of the United States.

FIRST CAUSE OF ACTION.

For its First Cause of Action plaintiff states:

1. Plaintiff is a corporation organized and existing under the laws of the State of New York with its principal office and place of business in the Town of Wheatfield, Niagara County, New York.

2. Plaintiff was organized and commenced business in 1935 and thereafter, during all the times mentioned herein, the major part of plaintiff's business has been the development and manufacture of military aircraft.

2 3. On August 14, 1941, plaintiff entered into Contract No. W535 ac-20910 with the defendant represented by Ennis McCall, First Lieutenant, United States Army Air Corps, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally known as, and hereinafter referred to as, a cost-plus-a-fixed-fee contract. A copy of the pertinent parts of said contract is attached hereto marked Exhibit A. Certain terms of the contract were altered from time to time by change orders and supplemental agreements, none of which is pertinent to this suit, except

the termination settlement agreement hereinafter referred to. The said contract was terminated by the defendant for its convenience on August 14, 1945, and thereafter, under date of December 21, 1945, plaintiff and defendant entered into a settlement agreement pursuant to the Contract Settlement Act of 1944, wherein the rights and liabilities of the parties under said contract were settled and determined, except the rights and liabilities with respect to certain excepted claims, including the claim alleged in this first cause of action.

4. Plaintiff, in accordance with the terms of said contract, furnished defendant with the military aircraft required by the said contract to be furnished by plaintiff to defendant and duly performed all the conditions required by it by said contract.

5. Defendant accepted the military aircraft furnished by plaintiff pursuant to said contract.

3 6. In the years 1938, 1939 and 1940, plaintiff performed three experimental fixed price contracts for the United States Government for the manufacture and delivery of certain experimental military airplanes known as Model XFN 1 (the "Airacuda"), Model XP 39 (the "Airacobra"), and Model XFL 1 (the "Airabonita"). One experimental airplane was manufactured under each contract. In the development of the three experimental airplanes, plaintiff expended for experimental and development work, the sum of $1,499,739.23 over and above the total contract price for the three airplanes. This amount was set up in a deferred experimental and development account for future amortization. The Company has amortized this deferred experimental and development cost over all airplanes which have been manufactured by it since the performance of the aforedescribed experimental contracts which have included principles of design developed in the performance of said experimental contracts.

7. The airplanes manufactured under Contract No. W535 ac-20910 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

8. Under the terms of Contract No. W535 ac-20910 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performin the contract the sum of $370,552.30, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. W535 ac-20910 up to and including August 31, 1943. Plaintiff alleges that the experimental and development costs included in said

vouchers were reimbursable costs of performing the said contract.

4 9. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 to be amortized over future production. The tooling acquired in the course of this program was used in the production of all P-39 airplanes produced by plaintiff, and upon the termination of plaintiff's contracts for said P-39 airplanes in the years 1944 and 1945, was treated by the defendant as its property and was disposed of as defendant's property pursuant to defendant's instructions.

10. The plaintiff has amortized said tooling costs over all airplanes on which the tooling acquired, as aforesaid, was used.

11. Under the terms of Contract No. W535 ac-20910, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $819,571.64. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. W535 ac-20910 up to and including August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

12. The defendant's contracting officer, pursuant to the authority vested in him by the terms of said contract, duly determined that the said amount of $1,190,123.94, the total amount of
5 deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-20910 up to and including August 31, 1943, were reimbursable costs of performing said contract under the terms thereof, and plaintiff was reimbursed for them. Thereafter, the General Accounting Office erroneously determined that said costs were not so reimbursable and defendant recouped said amount by deducting the same from sums otherwise due and owing the plaintiff from the defendant.

13. Under the terms of Contract No. W535 ac-20910, plaintiff also submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $194,947.81, representing the portion of said amortized experimental and

development costs allocable to the airplanes manufactured under Contract No. W535 ac-20910 subsequent to August 31, 1943, and the sum of $79,991.20 representing the portion of said tooling costs similarly allocable.

14. The defendant has refused to pay plaintiff the amount of $274,939.01, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-20910 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost for performing said contract.

15. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental and development and tooling costs over airplanes produced under fixed price contracts then on hand. In 1942, at which time defendant was performing Contract
6 No. W535 ac-20910 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. W535 ac-20910 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It therefore, disallowed $2,286,819.95 of the experimental, development and tooling costs as a business expense allocable to the performance of fixed price contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. W535 ac-20910 and other cost-plus-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed price contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury dis-

7 allowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. W535 ac-20910 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $274,939.01 for reimbursement of experimental, development and tooling costs allocable to airplanes produced under Contract No. W535 ac-20910 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War. The said appeal was heard and considered by the War Department Board of Contract Appeals, as the representative of the Secretary of War and the said Board affirmed the contracting officer's determination by decision dated April 29, 1946. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946. The administrative action taken with respect to the aforesaid $1,190,123.94 of experimental, development and tooling costs allocable to said contract during the period up to and including August 31, 1943, is set forth in paragraph 12 above.

16. The plaintiff is justly entitled to recover from the defendant the sum of $274,939.01 on account of experimental,
8 development and tooling costs allocable to Contract No. W535 ac-20910 subsequent to August 31, 1943, and the sum of $1,190,123.94 on account of such costs allocable to said contract up to and including August 31, 1943.

17. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and off-sets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

SECOND CAUSE OF ACTION.

18. Plaintiff incorporates herein by reference the allegations contained in paragraphs 1 and 2 of its First Cause of Action.

19. On September 10, 1941, plaintiff entered into Contract No. DA-W535 ac-156 with the defendant represented by R. H. Wheat, Major, United States Army Air Corps, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally known as, and hereinafter referred to as a cost-plus-a-fixed-fee contract.

A copy of the pertinent parts of said contract is attached hereto and marked Exhibit C. Certain terms of the contract were
9 altered from time to time by change orders and supplemental agreements, none of which is pertinent to this suit.

20. Plaintiff incorporates herein by reference the allegations contained in paragraphs 4, 5 and 6 of its first cause of action.

21. The airplanes manufactured under Contract No. DA-W535 ac-156 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

22. Under the terms of Contract No. DA-W535 ac-156 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $37,318.96, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. DA-W535 ac-156 up to and including August 31, 1943. Plaintiff alleges that the experimental and development costs included in said vouchers were reimbursable costs of performing the said contract.

23. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 of the "First Cause of Action" to be amortized over future production. The tooling acquired in the course of this program was used in the Production of all P-39 airplanes produced by plaintiff, and upon the termination of plaintiff's contracts for said P-39 air-
10 planes in the years 1944 and 1945, was treated by the de-

fendant as its property and was disposed of as defendant's property pursuant to defendant's instructions.

24. The plaintiff has amortized said tooling costs over all airplanes on which the tooling acquired, as aforesaid, was used.

25. Under the terms of Contract No. DA-W535 ac-156, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $72,413.12. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. DA-W535 ac-156 up to and including August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

26. The defendant's contracting officer, pursuant to the authority vested in him by the terms of said contract, duly determined that the said amount of $109,732.08, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. DA-W535 ac-156 up to and including August 31, 1943, were reimbursable costs of performing said contract under the terms thereof, and plaintiff was reimbursed for them. Thereafter, the General Accounting Office erroneously determined that said costs were not so reimbursable and defendant recouped said amount by deducting the same from sums otherwise due and owing the plaintiff from the defendant.

27. Under the terms of Contract No. DA-W535 ac-156, plaintiff also submitted to defendant cost vouchers which included as
11 a reimbursable cost of performing the contract the sum of $13,888.85, representing the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. DA-W535 ac-156 subsequent to August 31, 1943, and the sum of $4,371.50 representing the portions of said tooling costs similarly allocable.

28. The defendant has refused to pay the plaintiff the amount of $18,260.35, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. DA-W535 ac-156 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost of performing said contract.

29. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental, development and tooling costs over air-

planes produced under fixed price contract then on hand. In 1942, at which time defendant was performing Contract No. DA-W535 ac-156 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. DA-W535 ac-156 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It, therefore, disallowed $2,286,819.95 of the experimental development and tooling costs as a business expense allocable
12 to the performance of fixed price contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. DA-W535 ac-156 and other cost-plus-a-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed price contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury disallowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. DA-W535 ac-156 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $18,260.35 for reimbursement of experimental, de-
13 velopment and tooling costs allocable to airplanes produced under Contract No. DA-W535 ac-156 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War. The said ap-

peal was heard and considered by the War Department Board of Contract Appeals, which reported its decision affirming the decision of the Contracting Officer to the President of said Board as the authorized representative of the Secretary of War, whose decision was in accord therewith. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946. The administrative action taken with respect to th.. aforesaid $109,732.08 of experimental, development and tooling costs allocable to said contract during the period up to and including August 31, 1943, is set forth in paragraph 26 above.

30. The plaintiff is justly entitled to recover from the defendant the sum of $18,260.35 on account of experimental, development and tooling costs allocable to Contract No. DA-W535 ac-156 subsequent to August 31, 1943, and the sum of $109,732.08 on account of such costs allocable to said contract up to and including August 31, 1943.

31. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and offsets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

14

THIRD CAUSE OF ACTION.

32. Plaintiff incorporates herein by reference the allegations contained in paragraphs 1 and 2 of its first cause of action.

33. On June 29, 1942, plaintiff entered into Contract No. W535 ac-29318 with the defendant represented by Joseph E. Derham, Lieutenant Colonel, United States Army Air Forces, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally referred to as a cost-plus-a-fixed-fee contract. A copy of the pertinent parts of said contract is attached hereto and marked Exhibit D. Certain terms of the contract were altered from time to time by change orders and supplemental agreements, of which the following are pertinent to this suit:

(1) Supplemental Agreement No. 2, dated September 29, 1942, whereby the model airplane to be furnished was changed from Army Air Forces Model P-39-E to Model P-63A-1;

(2) Supplemental Agreement No. 37, dated April 13, 1945, whereby Contract No. W535 ac-40041 to which a portion of
15 said costs were originally allocable, was combined with and merged into Contract W535 ac-29318.

(3) Supplemental Agreement No. 64, dated May 15, 1946, which is the termination settlement agreement referred to below.

The said contract was terminated by the defendant for its convenience on August 14, 1945, and thereafter, under date of May 15, 1946, plaintiff and defendant entered into a settlement agreement, pursuant to the Contract Settlement Act of 1944, whereby the rights and liabilities of the parties under said contract were settled and determined, except the rights and liabilities with respect to certain excepted items, including the claim alleged in this third cause of action.

34. Plaintiff, in accordance with the terms of said contract, furnished defendant with the military aircraft required by the said contract to be furnished by plaintiff to defendant and duly performed all the conditions required of it by said contract.

35. Defendant accepted the military aircraft furnished by plaintiff pursuant to said contract.

36. In the years 1938, 1939 and 1940, plaintiff performed three experimental fixed price contracts for the United States Government for the manufacture and delivery of certain experimental military airplanes known as Model XFN 1 (the "Airacuda"), Model XP 39 (the "Airacobra"), and Model XFL 1 (the "Airabonita"). One experimental airplane was manufactured under each contract. In the development of the three experimental airplanes, plaintiff expended for experimental and development work, the sum of $1,499,739.23 over and above a total contract
16 price for the three airplanes. This amount was set up in a deferred experimental and development account for future amortization. The Company has amortized this deferred experimental and development cost over all airplanes which have been manufactured by it since the performance of the aforedescribed experimental contracts which have included principles of design developed in the performance of said experimental contracts.

37. The airplanes manufactured under Contract No. W535 ac-29318 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

38. Under the terms of Contract W535 ac-29318 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $223,288.09, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. W535 ac-29318 subsequent to August 31, 1943. Plaintiff alleges that the experimental and development costs included in said vouchers were reimbursable costs of performing the said contract.

39. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 of the First Cause of Action to be amortized over future production. The tooling acquired in the course of this program was used in
17 the production of all P-39 airplanes produced by plaintiff, and upon the termination of paintiff's contracts for said P-39 airplanes in the years 1944 and 1945, was treated by the defendant as its property and was disposed of as defendant's property pursuant to defendant's instructions.

40. The plaintiff has amortized said tooling costs over all airplanes on which tooling acquired, as aforesaid, was used.

41. Under the terms of Contract No. W535 ac-29318, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $69,895.04. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. W535 ac-29318 subsequent to August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

42. The defendant has refused to pay plaintiff the amount of $293,183.13, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-29318 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost for performing said contract.

43. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental, development and tooling costs over

airplanes produced under fixed price contracts then on hand. In 1942, at which time defendant was performing Contract
18 No. W535 ac-29318 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. W535 ac-29318 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It, therefore, disallowed $2,286,819.95 of the experimental, development and tooling costs as a business expense allocable to the performance of fixed price contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. W535 ac-29318 and other cost-plus-a-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed price contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury
19 disallowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. W535 ac-29318 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $293,183.13 for reimbursement of experimental, development and tooling costs allocable to airplanes produced under Contract No. W535 ac-29318 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that the plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War.

The said appeal was heard and considered by the War Department Board of Contract Appeals as, the representative of the Secretary of War, and the said Board affirmed the contracting officer's determination by decision dated April 29, 1946. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946.

44. The plaintiff is justly entitled to recover from the defendant the sum of $293,183.13 on account of experimental, development and tooling costs allocable to Contract No. W535 ac-29318.

45. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said
20 claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and offsets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

FOURTH CAUSE OF ACTION.

46. Plaintiff incorporates herein by reference the allegations contained in paragraphs 1 and 2 of its first cause of action.

47. On September 28, 1943, plaintiff entered into Contract W535 ac-40071 with the defendant represented by Robert A. Watson, Captain, United States Air Corps, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally referred to as a cost-plus-a-fixed-fee contract. A copy of the pertinent parts of said contract is attached hereto and marked Exhibit E. Certain terms of the contract were altered from time to time by change orders and supplemental agreements, of which the following are pertinent to this suit; (1) Change Order No. 3 dated December 24, 1943, a copy of the pertinent part of which is included in Exhibit E; (2) Supplemental Agreement No. 36, dated February 22, 1946, which is the termination settlement agreement referred to below.

21 The said contract was terminated by the defendant for its convenience on August 14, 1945, and thereafter under

date of February 22, 1946, plaintiff and defendant entered into a settlement agreement pursuant to the Contract Settlement Act of 1944, whereby the rights and liabilities of the parties under said contract were settled and determined, except the rights and liabilities with respect to certain excepted items, including the claim alleged in this Fourth Cause of Action.

48. Plaintiff, in accordance with the terms of said contract, furnished defendant with the military aircraft required by the said contract to be furnished by plaintiff to defendant and duly performed all the conditions required of it by said contract.

49. Defendant accepted the military aircraft furnished by plaintiff pursuant to said contract.

50. In the years 1938, 1939 and 1940, plaintiff performed three experimental fixed price contracts for the United States Government for the manufacture and delivery of certain experimental military airplanes known as Model XFN 1 (the "Airacuda"), Model XP 39 (the "Airacobra"), and Model XFL 1 (the "Airabonita"). One experimental airplane was manufactured under each contract. In the development of the three experimental airplanes, plaintiff expended for experimental and development work, the sum of $1,499,739.23 over and above a total contract price for three airplanes. This amount was set up in a deferred experimental and development account for future amortization. The Company has amortized this deferred experimental and development cost over all airplanes which have been manufactured
22 by it since the performance of the aforedescribed experimental contracts which have included principles of design developed in the performance of said experimental contracts.

51. The airplanes manufactured under Contract No. W535 ac-40071 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

52. Under the terms of Contract No. W535 ac-40071 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $195,922.72, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. W535 ac-40071 subsequent to August 31, 1943. Plaintiff alleges that the experimental and development costs included in said vouchers were reimbursable costs of performing the said contract.

53. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production

requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 of the First Cause of Action to be amortized over future production. The tooling acquired in the course of this program was used in the production of all P-39 airplanes produced by plaintiff, and upon the termination of plaintiff's contracts for said P-39 airplanes in the years 1944 and 1945, was treated by the defendant as
23 its property and was disposed of as defendant's property pursuant to defendant's instructions.

54. The plaintiff has amortized said tooling costs over all airplanes on which the tooling acquired, as aforesaid, was used.

55. Under the terms of Contract No. W535 ac-40071, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $204,658.72. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. W535 ac-40071 subsequent to August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

56. The defendant has refused to pay plaintiff the amount of $400,581.44, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-40071 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost for performing said contract.

57. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental, development and tooling costs over airplanes produced under fixed price contracts then on hand. In 1942, at which time defendant was performing Contract No. W535 ac-40071 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the
24 Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. W535 ac-40071 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It, therefore, disallowed $2,286,819.95 of the experimental, development and tooling costs as a business expense allo-

cable to the performance of fixed priced contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. W535 ac-40071 and other cost-plus-a-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury disallowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. W535 ac-40071 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $400,581.44 for reimbursement of experimental, development and tooling costs allocable to airplanes produced under Contract No. W535 ac-40071 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War. The said appeal was heard and considered by the War Department Board of Contract Appeals, as the representative of the Secretary of War, and the said Board affirmed the contracting officer's determination by decision dated April 29, 1946. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946.

58. The plaintiff is justly entitled to recover from the defendant the sum of $400,581.44 on account of experimental, development

and tooling costs allocable to Contract No. W535 ac-40071 subsequent to August 31, 1943.

59. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and off-sets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

WHEREFORE, plaintiff prays judgment against the United States on the four causes of action contained in this petition in the sum of $2,286,819.95.

DUDLEY, STOWE & SAWYER,
Attorneys for
Bell Aircraft Corporation,
Manufacturers & Traders Building,
Buffalo, New York

COVINGTON, BURLING, RUBLEE,
ACHESON & SHORB,
Union Trust Building,
Washington, D. C.
Of Counsel.

Exhibit A to Petition

Pertinent portions of Contract No. W535 ac-20910

ARTICLE 1—*Statement of Work*

(a) The Contract shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item (1)—Eighteen Hundred (1800) Airplanes, Interceptor Pursuit, Single-Place, Single-Engine, Contractor's type and Model 15, being known and designated as Air Corps' Type and Model P-39-D, as completed and manufactured in accordance with Bell Aircraft Corporation Model Specification No. 4Y003J, dated July 30, 1941, hereby made a part hereof.

(This article contains additional provisions for the furnishing of spare parts and technical data which are omitted)

ARTICLE 3—*Consideration*

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the contract, subject to reimbursement for cost as outlined in Article 6 hereof, the cost, plus a fixed fee of Four Million Two Hundred Fifty-Seven Thousand Six Hundred Forty Four Dollars and Forty Cents ($4,257,644.40) being six percent of the total estimated cost of Seventy Million Nine Hundred Sixty Thousand and Seven Hundred Forty Dollars ($70,960,740.00). This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

29 (b) For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing that

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract, would have been considered as allowable items of cost within the meaning of said regulations, shall be considered as allowable items of cost incurred hereunder.

(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this contract, notwithstanding any provision contained in the specifications or other documents incorporated in this contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense or without cost to the Government.

In the event that prior to final settlement under this contract such regulations be amended so as to provide for additional allowable items of cost such additional items shall be considered allowable items hereunder.

(c) The Contractor shall, to the extent of his ability, procure materials and services at the most advantageous prices available with due regard to securing prompt delivery of satisfactory materials, take all cash and trade discounts, rebates, allowances, credits, salvage, commissions and bonifications, and when unable to take advantage of such benefits he shall promptly notify the Contracting Officer to that effect and the reason therefor. In determining the actual net cost of articles and materials of every kind required for the purpose of this contract, there shall be deducted from the gross cost thereof all cash and trade discounts, rebates, allowances, credits, salvage, commissions and bonifications which have accrued to the benefit of the Contractor or would have so accrued except for the fault or neglect of the Contractor. Such benefits lost through no fault or neglect on the part of the Contractor, or lost through fault of the Government, shall not be deducted from gross costs.

ARTICLE 6—*Payments*

(a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 as may be approved or ratified and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers. Provided, however, that subject to the requirement of paragraph (c) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this article. Generally, reimbursement will be made weekly but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 16—*Disputes*

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his

decision to writing and mail a copy thereof to the Con-
31 tractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or the president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum
or sums allowed to the Contractor under the provisions of
32 this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

EXHIBIT B TO PETITION.

September 7, 1943

Price Adjustment Board
War Department, I T & T Building
67 Broad Street
New York, New York

Dear Sirs:

Attention: Major Knox B. Phagan

Pursuant to our telephone conversation this afternoon, we should be glad if you would indicate your approval of the method to be followed in amortizing development and experimental expenses and production tooling costs of P-39 airplanes.

Our records as of December 31, 1942 and the schedules originally submitted to you showed that we had amortized the full amount of these costs against fixed price contracts. You objected to such treatment on the ground that the costs should be amortized over cost plus a fixed fee as well as fixed price contracts. The Bureau of Internal Revenue in examining our Federal income and excess profits tax return for the calendar year 1941 had made the same objection and required us to amortize the costs over all airplane contracts then held by us. In view of the position taken by the Bureau of Internal Revenue and yourselves we have agreed to amortize the experimental and development expenditures over all contracts for P-39 and P-63 airplanes and the P-39 production tooling expenditures over all contracts for P-39 airplanes, provided that, the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office. Under date of August 14, 1943 we
33 provided you with two schedules which set forth in detail the amounts and contracts involved in the writeoff from January 1, 1940 to June 30, 1943 on an actual writeoff basis and through the balance of 1943 and 1944 on an estimated basis.

The method agreed upon involved a determination of each of the two amounts involved, which amounts are as shown by our books (and less adjustments aggregating $2,892.19 are as shown by a report of an Agent of the Bureau of Internal Revenue as of December 31, 1940) less adjustments made by the Contract Audit Section of the Army Air Forces as a result of their examination of their costs. The amounts are as follows:

Price Adjustment Board
Attention: Major Knox B. Phagan

September 8, 1943.

	Development and Experimental	P-39 Production Tooling	Together
Costs to December 31, 1940 (there were no additions subsequently)	$1,528,760.66	$1,894,109.57	$3,422,870.23
Less—Costs disallowed by Contract Audit Section, Army Air Forces	29,021.43	19,383.80	48,405.23
Amount to be amortized as agreed upon with Price Adjustment Board and Contract Audit Section, Army Air Forces	$1,499,739.23	$1,874,725.77	$3,374,465.00

The last amounts shown above are to be amortized over all fixed price and cost plus a fixed fee supply contracts for P-39 and P-63 airplanes as follows:

The sum of the number of airplanes and equivalents on order and undelivered at the beginning of the year and the number of airplanes and equivalents ordered during the calendar year is to be divided into the unamortized costs as of the beginning of the year, the resulting quotient represents the amortization per airplane. The amortization per airplane
34 multiplied by the number of airplanes and equivalents accepted by the Army Air Forces during the period of each contract results in the amortization per contract.

We believe the foregoing sets the understanding between us as to the amortization of the expenditures for exprimental and development and P-39 production tooling and if it is in accordance with your understanding we should like you to so indicate by signing one copy of this letter and returning it to us.

Yours very truly,

BELL AIRCRAFT CORPORATION
JOHN BERRY, JR. /s/
JOHN BERRY, JR.
Comptroller

JB,Jr:rla

The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

Signed: KNOX B. PHAGAN
Major A. C.
Price Adj. Officer
Date: Sept. 9, 43

EXHIBIT C TO PETITION.

Pertinent portions of Contract No. DA-W535 ac-156

ARTICLE 1—*Statement of Work*

(a) The Contractor shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item 1—Two Hundred (200) Airplanes, Pursuit, Single-Place, Single-Engine, Contractor's type and Model 14, being known and designated as Air Corps Model P-39D-1, as constructed in accordance with Bell Aircraft Corporation Specification No. 14-945-001-1 dated May 20, 1941, packed for overseas shipment.

Item 2—One Hundred Forty-Four (144) Airplanes Pursuit, Single-Place, Single-Engine, Contractor's type and Model 14, being known and designated as Air Corps Model P-39D-1, as constructed in accordance with Bell Aircraft Corporation Specification No. 14-945-001-1, dated May 20, 1941, set up and serviced for fly-away at Contractor's flying field.

(Additional provisions covering the furnishing of spare parts and data are omitted)

ARTICLE 3—*Consideration*

(a) The Government will pay the contractor upon satisfactory delivery of all items specified in the contract, subject to reimbursement for costs as outlined in Article 6 hereof, the cost, plus a fixed fee of Eight Hundred Ninety-Nine Thousand One Hundred Fifty-Five and 56/100 Dollars ($899,155.56), being Six percent of the total estimated cost of Fourteen Million Nine Hundred Eighty Five Thousand Nine Hundred Twenty-Six dollars ($14,985,926.00). This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

(b) For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for determination of the cost of performing a contract as promulgated by the

Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being
36 understood and agreed without limiting the generality of the foregoing that:

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract would have been considered as allowable items of cost within the meaning of this article shall be allowable items of cost hereunder;

(2) Any cost incurred by the Contractor under the terms of this contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this contract notwithstanding any provisions contained in the specifications or other documents incorporated in this contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense without cost to the Government.

(c) In the event that prior to final settlement under this contract, the above-mentioned regulations (T. D. 5000) shall have been amended either on or before the effective date of this contract so as to provide for additional allowable items of cost, such additional items shall be considered allowable items hereof.

ARTICLE 6—*Payments*

(a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 as may be approved or ratified and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers. Provided, however, that subject to the requirement of paragraph (c) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer
37 with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this article. Generally, reimbursement will be made weekly but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 16—*Disputes*

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

EXHIBIT D TO PETITION.

Pertinent portions of Contract No. W535 ac-29318

ARTICLE 1—*Statement of Work*

(a) The Contractor shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item 1—Two Thousand (2000) airplanes, Intereceptor Pursuit, single place, single engine, Contractor's Type and Model 28, Air Corps Type and Model P-39-E, each complete and conforming to Contractor's Specification No. 28-947-001, dated January 14, 1942, hereby made a part hereof.
(This article contains additional provisions for the furnishing of spare parts and technical data which are omitted)

ARTICLE 3—*Consideration*

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in this contract, subject to
38 reimbursements for cost, as outlined in Article (6) hereof, the cost, plus a fixed fee of Three Million Five Hundred Forty-six Thousand Eight Hundred Dollars and no cents ($3,546,800.00) being four per cent (4%) of the total estimated cost of Eighty-eight Million Six Hundred Seventy Thousand Dollars and no cents ($88,670,000.00). This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof; provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

(b) For purposes of determining the amounts payable to the Contractor under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for the determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter I of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War, August 2, 1940, it being understood and agreed, without limiting the generality of the foregoing, that:

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract would have been considered as allowable items of cost within the meaning of this article, shall be allowable items of cost hereunder.

(2) Interest on unreimbursed portions of actual investments in a facility or facilities used for the performance of this contract and acquired pursuant to any Emergency Plant Facilities Contract or Contracts with the Government, now in effect or hereafter entered into, including any amendment thereof, at the rate or rates provided for in the Emergency
39 Plant Facilities Contract or Contracts involved shall be an allowable cost hereunder to the extent that such interest accrues during the performance of this contract; provided, that if the facility or facilities also are used concurrently for the perfomance of another contract or contracts, only so much of such interest as is proportionate to the use of the facility or facilities for the performance of this contract shall be an allowable cost hereunder; and, provided further, that such interest shall not be an allowable cost hereunder to the extent that such interest is allowed as a cost under any other contract or contracts.

(3) Cost of such bonds and insurance as the Contracting Officer may approve or require and cost and expenses incurred in the defense and/or discharge of such claims of others on account of death or bodily injury of persons or loss or destruction of or damage to property as may arise out of or in connection with the performance of the work under this contract shall be an allowable item of cost hereunder, provided that such reimbursement shall not include any amount for which the Contractor is indemnified or compensated by insurance or otherwise, or any amount for which it would have been so indemnified or compensated except for the failure of the Contractor to procure or maintain bonds

or insurance in accordance with the requirements of the Contracting Officer. The foregoing shall not restrict the right of the Contractor to be reimbursed for the cost of insurance covering the Contractor's property or property for which the Contractor is responsible to someone other than the Government and which is used or to be used in the performance of this contract.

ARTICLE 6—*Payments*

a) *Reimbursement for Cost.*—The Government will currently reimburse the Contractor for such expenditures made in ac-
40 cordance with Article 3 hereof as may be approved or ratified by the Contracting Officer, and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; provided, however, that subject to the requirement of paragraph (b) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event in be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this Article. Generally, reimbursement will be made weekly, but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 9—*Termination of Contract by Government.*

(b) Upon the termination of this contract as hereinbefore provided, full and complete settlement of all claims of the Contractor arising out of this contract shall be made as follows:

(3)(a) The Government shall reimburse the Contractor for such further expenditures after the date of termination, if approved by the Contracting Officer as necessarily expended or incurred by the Contractor, as would, if incurred before such termination, have been considered as allowable items of cost within the meaning of T. D. 5000. To the extent that the Contracting Officer may find such further costs to have been necessarily expended or incurred by the Contractor, it is understood and agreed without limiting the generality of the foregoing that such further necessary expenditures may include rental charges during the period while Government property remains in the possession of the Contractor, wages of employees from the date of termination to the earliest date of layoff consistent with Collector's established pro-
41 cedure, separation payments to employees on account of

layoffs required by such termination made in accordance with collective bargaining contracts between the Contractor and the recognized representatives of its employees, deferred development costs, direct expense, general overhead expense and the cost of tools, jigs, dies, patterns, templates and fixtures not theretofore charged to the cost of sales, the costs of cancellation of subcontracts and purchase orders, and claims arising therefrom, the costs of storage, packing, transportation and delivery to the Government of Government property, and such other expenditures as the Contracting Officer may approve.

ARTICLE 16—*Disputes*

(Added by Supplemental Agreement No. 2, dated September 29, 1942)

Except as otherwise specifically provided in this contract all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or
42 of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or the president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any

division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

Whenever in any other Article of this Contract any reference is made to Article 16, such reference shall be deemed to be to the foregoing provisions of this Article.

43

EXHIBIT E TO PETITION. t

Pertinent Portions of Contract No. W535 ac-40071

ARTICLE 1—*Statement of Work*

The Contractor shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item 1—Two Thousand (2,000) Airplanes, Fighter, Single Engine, Single Place, Contractor's Type and Model 26E series, Army Air Forces Type and Model P-39Q Series, Each complete and conforming to Contractor's Specification No. 4Y003J-Q10 dated 24 April 1943, hereby made a part hereof.
(This article contains additional provisions for the furnishing of spare parts and technical data which are omitted.)

ARTICLE 3—*Consideration*

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in this contract, subject to reimbursements for cost, as outlined in Article (6) hereof, the cost, plus a fixed fee of Two Million Seven Hundred Thirty-five Thousand Four Hundred Eighty-eight Dollars and No Cents ($2,735,488.00) being four per cent (4%) of the total estimated cost of Sixty-eight Million Three Hundred Eighty-seven Thousand Two

Hundred Dollars and No Cents ($68,387,200.00) as set forth in Article 2. This estimated cost and the fixed fee are subject to increases or decreases as provided herein. There shall be no adjustment in the amount of the fixed fee, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost or because of the fact that the estimated cost varies from the actual cost.

44 (b) For the purposes of determining the amounts payable to the Contractor under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for the determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter I of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War, August 2, 1940, it being understood and agreed, without limiting the generality of the foregoing, that:

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract would have been considered as allowable items of cost within the meaning of this Article, shall be allowable items of cost hereunder.

(2) Interest on unreimbursed portions of actual investments in a facility or facilities used for the performance of this contract and acquired pursuant to any Emergency Plant Facilities Contract or Contracts with the Government, now in effect or hereafter entered into, including any amendment thereof, at the rate or rates provided for in the Emergency Plant Facilities Contract or Contracts involved, shall be an allowable cost hereunder to the extent that such interest accrues during the performance of this contract; provided, that if the facility or facilities also are used concurrently for the performance of another contract or contracts, only so much of such interest as is proportionate to the use of the facility or facilities for the performance of this contract shall be an allowable cost hereunder; and, provided further, that such interest shall not be an allowable cost hereunder to the extent that such interest is allowed as a cost under any other contract or contracts.

45 (3) Cost of such bonds and insurance as the Contracting Officer may approve or require and cost and expenses incurred in the defense and/or discharge of such claims of others on account of death or bodily injury of persons or

loss or destruction of or damage to property as may arise out of or in connection with the performance of the work under this contract shall be an allowable item of cost hereunder, provided that such reimbursement shall not include any amount for which the Contractor is indemnified or compensated by insurance or otherwise, or any amount for which it would have been so indemnified or compensated except for the failure of the Contractor to procure or maintain bonds or insurance in accordance with the requirements of the Contracting Officer. The foregoing shall not restrict the right of the Contractor to be reimbursed for the cost of reasonable insurance covering the Contractor's property or property for which the Contractor is responsible to someone other than the Government and which is used or to be used in the performance of this contract.

ARTICLE 6—*Payments*

(a) *Reimbursement for Cost.*—The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer, and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; provided, however, that subject to the requirement of paragraph (b) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Con-
46 tracting Officer, covering expenditures to be reimbursed under this Article. Generally, reimbursement will be made weekly, but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 9—*Termination of Contract by Government.*

(b) Upon the termination of this contract as hereinbefore provided, full and complete settlement of all claims of the Contractor arising out of this contract shall be made as follows:

(3) (a) The Government shall reimburse the Contractor for such further expenditures after the date of termination, if approved by the Contracting Officer as necessarily expended or incurred by the Contractor, as would, if incurred before such termination, have been considered as allowable items of cost within the meaning of

T. D. 5000. To the extent that the Contracting Officer may find such further costs to have been necessarily expended or incurred by the Contractor, it is understood and agreed without limiting the generality of the foregoing that such further necessary expenditures may include rental charges during the period while Government property remains in the possession of the Contractor, wages of employees from the date of termination to the earliest date of layoff consistent with the Contractor's established procedure, separation payments to employees on account of layoffs required by such termination made in accordance with collective bargaining contracts between the Contractor and the recognized representatives of its employees, deferred development costs, direct expense, general overhead expense and the cost of tools, jigs, dies, sales, the cost of cancellation of subcontracts and purchase orders, and claims arising therefrom, the costs of storage, packing, transportation and delivery to the Government of Government property, and such other expenditures as the Contracting Officer may approve.

The foregoing excerpt from Article 9(b) was amended by Change Order No. 3 dated December 17, 1943, to read as follows:

47 "(a) The Government shall reimburse the Contractor for such further expenditures after the date of termination, if approved by the Contracting Officer as necessarily expended or incurred by the Contractor as would if incurred before such termination, have been considered as allowable items of cost within the meaning of T. D. 5000. To the extent that the Contracting Officer may find such further costs to have been necessarily expended or incurred by the Contractor, it is understood and agreed without limiting the generality of the foregoing that such further necessary expenditures may include rental charges during the period while Government property remains in the possession of the Contractor, wages of employees from the date of termination to the earliest date of layoff consistent with Contractor's established procedure, separation payments to employees on account of layoffs required by such termination made in accordance with collective bargaining contracts between the Contractor and the recognized representatives of its employees, deferred development costs, direct expense, general overhead expense, and the cost of tools, jigs, dies, patterns, templates and fixtures not theretofore charged to the cost of sales, the cost of cancellation of subcontracts and purchase orders, and claims arising therefrom, the costs of storage, packing, transportation and delivery to the Government of Government property, and such other expenditures as the Contracting Officer may approve."

REASON: To correct a typographical error.

ARTICLE 16—*Disputes*

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto.

48 The Secretary of War may, in his discretion, designate an individual, or individuals other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

49 **GENERAL TRAVERSE—Filed Aug. 18, 1947.**

And now comes the Attorney General, on behalf of the United States, and answering the petition of the claimant herein, denies each and every allegation therein contained; and asks judgment that the petition be dismissed.

/s/ HERBERT A. BERGSON
Acting Assistant Attorney General.

JBM
HAB

51 IN THE UNITED STATES COURT OF CLAIMS

No. 47745

Filed May 18, 1950

BELL AIRCRAFT CORPORATION

v.

THE UNITED STATES

REPORT OF COMMISSIONER—Filed May 18, 1950

To the Honorable the CHIEF JUDGE AND ASSOCIATE JUDGES OF THE UNITED STATES COURT OF CLAIMS:

Pursuant to the order of reference in the above-entitled case, the undersigned commissioner herewith makes the following report of his findings of fact:

1. The plaintiff is a corporation organized and existing under the laws of the State of New York with its principal office and place of business in the Town of Wheatfield, Niagara County, New York.

2. The plaintiff was organized and commenced business in 1935, and thereafter, during all the times mentioned herein, the major part of the plaintiff's business has been the development and manufacture of military aircraft.

EXPERIMENTAL AND DEVELOPMENT COSTS DEFERRED

3. In 1936, 1937, and 1938, the plaintiff entered into certain experimental contracts with the defendant, through the United States Army Air Corps for the construction of certain experimental and service test airplanes. Experimental airplanes were designated by the letter "X" preceding the model number, and the service test airplanes were designated by the letter "Y" preceding the model number. Other designations of type preceding the model number of particular airplanes hereinafter mentioned were "F" for "Fighter" and "P" for "Pursuit."

52 4. The following fixed-price experimental contracts were entered into between the plaintiff and the United States for fighter planes, in the performance of which the plaintiff incurred substantial expenditures over and above amounts received, which costs were set up on the plaintiff's books as deferred charges applicable to anticipated future production:

Item	Date of contract	Contract numbers	Airplanes Units	Models	Designations	Contract price
(A)	5/12/36	W 535 ac-8773	1	XFM-1	"Airacuda"	$ 390,000
(B)	9/27/37	W 535 ac-10341 ...	1	XP-39	"Airacobra"	245,000
(C)	4/20/38	W 535 ac-11122 ...	10	YFM-1	"Airacuda"	3,168,350
			3	YFM-1A		
(D)	11/ 8/38	63629	1	XFL-1	"Airabonita"	245,000
			16			4,049,446

The foregoing contracts are referred to in paragraphs 3 to 6, inclusive, of the stipulation between counsel (Plaintiff's Exhibit 1) and designated as Exhibits A to D, inclusive, to such stipulation. They are incorporated herein by reference. Contract No. 63629 was with the Navy, Bureau of Supplies and Accounts, and the others were with the Army Air Corps.

Articles 19, 21, 27, and 29, respectively, of the foregoing contracts provide for a nonexclusive, irrevocable right and license to the Government to use any and all discoveries, inventions, improvements and/or suggestions which are wholly or in part developed, perfected and/or reduced to practice with the aid and/or cooperation of the Government or of Government personnel, and/or by the contractor to meet explicit Governmental requirements or by the fulfillment of such contract.

Articles 26, 26 and 25, respectively, of the Army contracts provide:

> ***Reproduction rights.***—It is understood and agreed that the contractor does not convey to the Government any reproduction rights in or to the articles and/or spare parts called for herein by virtue of the terms of this contract, except as hereinbefore set forth.

53 The plaintiff acquired a number of basic patents in connection with its development work, on which substantial royalties were realized.

5. All the airplanes delivered on these experimental contracts, as well as the production contracts received later, were powered by liquid-cooled Allison engines, furnished by the Government. The Government also furnished other materials and parts, consisting of the wheels, tires, tubes, propellers, guns, instruments and certain electrical and communications equipment.

The Airacuda was a twin-engine, five-place, long-range fighter plane with pusher propellers operated by drive shafts to the engine. It was armed with two 37mm. repeating cannon, flexibly mounted in the nose of its engine nacelles, and two 50-calibre machine guns installed in the waist, with flexible mountings manually

operated, with a wide sweep firing range upward, downward or rearward. These planes were originally designed with conventional landing gear, that is, with two wheels abreast under each wing and a tail wheel to carry the rear portion of the fuselage. The three YFM-1A service test model Airacudas incorporated the tricycle landing gear which had been developed in connection with the experimental Airacobra.

The Allison engines supplied for the experimental planes operated at maximum power at sea level. The plaintiff installed an external General Electric turbo supercharger, driven from the engine, which increased its power at high altitudes. Allison later delivered altitude-rated engines, which duplicated the external unit and voided its further use. Two of the service test Airacudas incorporated the altitude-rated engines. The Airacuda was approximately two and one-half times the weight of the Airacobra.

The Airacobra was a single-engine and propeller, single-seat, short-range interceptor fighter plane. The engine, mounted to the rear of the cockpit, operated the propeller at the nose of the plane by means of a drive shaft. A tricycle landing gear was developed in the experimental model which consisted of a retractable nose wheel and two retractable wing wheels. The Airacobra was armed
with one 37mm. repeating cannon which fired through the
54 shaft and hub of the propeller from a fixed mounting, and
two 50-calibre machine guns which fired from fixed mountings between the propeller blades, so that the position of the plane governed the aim at a target, without any manual control.

The Airabonita was modeled after the Airacobra, but adapted to use on airplane carriers. The conventional landing gear was restored to this model and a tail hook was provided to engage the carrier deck arresting gear for landing purposes.

6. The first experimental Airacuda had been substantially completed by the end of 1937, and the excess of costs over the contract price for this unit was charged to profit and loss accounts for that year. Subsequent to the delivery of this airplane in 1938, the plaintiff incurred additional expenditures for the development and improvement in this design. The plaintiff's expenditures for the 13 test models of this design were also substantially in excess of the contract price received. These excess costs were capitalized as "deferred charges" in 1939 and 1940 for distribution as an element of cost against future production.

Much of the basic engineering and development designing in the Airacuda was carried forward and incorporated in the Airacobra which later entered quantity production for the Army Air Corps and the British Government.

The tooling for experimental contract work was of a temporary nature and fixtures for assembly were made of wood, very little of

which had any useful value for later production. All excess costs on experimental contracts were classified as experimental and development expense. Such costs were accumulated from year to year during the performance of the several experimental contracts. No segregation of these costs was made as to their application to the specific contracts on which excessive costs were incurred, except the first amount deferred in 1938, which resulted from work on the experimental contract for the Airacobra.

The plaintiff deferred and capitalized experimental and development costs as follows:

December 31, 1938	$ 128,052.77
December 31, 1939	511,776.21
December 31, 1940	888,931.68
Total	1,528,760.66

55 Although the deferred experimental and development costs were not segregated in the plaintiff's accounts in respect to the specific contracts under which excess costs were incurred, the plaintiff's auditors reported approximate allocations as follows:

Airacudas	$ 889,499.48
Airacobra	229,086.30
Airabonita	410,174.88
Total	1,528,760.66

The defendant's Army Audit Agency disallowed items totaling $29,021.43, leaving a balance of $1,499,739.23 in the deferred account for experimental and development expense, which sum represented the plaintiff's costs over and above the sums received under the contracts for experimental airplanes.

7. The plaintiff received no production contracts for any of the types described as Airacudas or the Airabonita airplanes. It received many contracts for great numbers of the Airacobra pursuit fighter plane, known as the P–39.

PRODUCTION TOOLING COSTS DEFERRED

8. On April 26, 1939, the plaintiff entered into contract W 535 ac–12635 with the Army Air Corps for the delivery of 13 service test models of the Airacobra with additional parts at a fixed price of $1,073,445. Twelve of these planes were described as YP–39, Model 4–C, and one YP–39A, Model 4–D.

The work under this contract was merged in the shop with production on later contracts, and any additional experimental costs in connection with its performance were absorbed in the production costs on fixed-price production contracts.

Thereafter, from time to time, the plaintiff was awarded additional production contracts for P–39 Airacobras with both the United States and the British Governments. The earlier production contracts were fixed price, and the later ones were cost-plus-fixed-fee contracts. Under the cost-plus-fixed-fee contracts, hereinafter referred to as CPFF contracts, the plaintiff was reimbursed for allowable costs of manufacture and was paid a fixed fee specified in the contract.

56 The production of P–39 Airacobras was continued on all of these contracts until April 1944, at which time the uncompleted contracts were amended to provide for deliveries of P–63 models. Numerous changes were made during the entire production period of the P–39 models to reduce costs and facilitate production, to avoid field breakage and to improve functional operations.

9. The plaintiff received the following fixed-price contracts for the production and delivery of Airacobra fighter planes:

Item	Date of contract	Contract numbers	Unit planes and equivalent in spare parts	Models	Contract price
United States					
(E)	4/26/39	W 535 ac-12635	13 1	YP-39 YP-39A	$1,073,445.00
(F)	9/30/39	W 535 ac-13383	87	P-39C	2,833,236.00
(G)	9/ 7/40	W 535 ac-15675 Increased	120 565	P-39D	4,962,220.00 21,276,912.79
(H)	6/ 5/41	W 535 ac-32	180	P-39D-1	7,407,540.00
			966		37,553,353.79
British					
	8/15/40	A-218	200	P-400	9,517,507.55
	10/ 8/40	A-1326	250	P-400	9,647,163.33
	10/10/40	A-1476	360	P-400	14,645,980.19
Totals			810		33,810,651.07
			1,776		71,364,004.86

The foregoing contracts are referred to in paragraphs 8 to 14, inclusive, of the stipulation of facts. The United States contracts were entered into with the Army Air Corps, copies of which are designated as Exhibits E to H to the stipulation and incorporated herein by reference.

The Model P–400 produced under British contracts was the British version of the P–39 and was of similar type and character as the Airacobra pursuit fighter planes specified under the contracts with the United States Army Air Corps.

The Army Air Corps contracts contain similar provisions, in respect to the right and license of the Government in any and
57 all discoveries, inventions and improvements, as those set

forth in Finding 4 for experimental contracts. These contracts also contain provisions substantially as follows:

> *Provisions Reference Section 14 of the Act Approved April 3, 1939—Limitation on Profits—It is expressly understood and agreed by both parties hereto that the contractor hereby agrees:*
>
> • • • • •
>
> (e) That the manufacturing spaces and books of its own plant, affiliates, and subdivisions shall at all times be subject to inspection and audit by any person designated by the Secretary of War, the Secretary of the Treasury and/or by a duly authorized committee of Congress.
>
> • • • • •
>
> *Cost Records.*—The contractor agrees to keep cost records in accordance with its own methods and practices of computing costs of all expenses incurred by it in connection with the performance of this contract and such records shall be available for inspection of the Contracting Officer or his representative after the completion or earlier termination of this contract. Such cost data shall be for the information of the Government, but shall in no way affect the contract price of the articles, spare parts, supplies or work covered by this contract.

10. About April 1939, when the plaintiff received its contract for the production of service test models of the P–39 Airacobra, it began to fabricate and install permanent tooling for the production of this type of airplane. Production tooling is distinguished from ordinary machine tools, in that the latter are more permanent and universal in character, consisting of milling machines, lathes, drill presses, etc., not restricted in use to specific models or types of the product manufactured.

Production tooling for the P–39 pursuit fighter plane was largely assembly tooling, consisting of long-beam assembly, subassembly and tail-assembly fixtures, all of which were fabricated in structural steel and remained in use as long as this type of plane was in production. It also included metal tubes, angles, form blocks, jigs, router templets and templet dies. In the production of ex-
58 perimental models, most of these fixtures were fabricated in wood, and tooling was provided for temporary use. But, in the production of service planes the plaintiff was required to provide for interchangeability of certain parts, such as wings, tails, and surface landing gear, necessitating accurate duplications of the various parts.

As additional contracts for Airacobras were received during 1939 and 1940, the plaintiff increased its numbers of assemblies to provide for greater production and duplicated the tooling for such assemblies, subassemblies, and such auxiliary tooling as became necessary to meet increased production requirements. The plaintiff provided tooling for its Niagara Falls plant, which started operations in June 1941, similar to that it had installed in its Elmwood Avenue plant.

During 1939 and 1940, the plaintiff incurred costs for production tooling for the P–39 Airacobra in the sum of $1,894,109.57. In December 1940, the plaintiff recorded this sum in a deferred account, together with the deferred costs on experimental contracts, entitled "Experimental, Development and Production Tooling Expenses." The defendant's Army Audit Agency disallowed $19,383.80 of the deferred cost for tooling, leaving $1,874,725.77 for allocation to future production.

11. In addition to the special production tooling set forth in the preceding finding, a substantial amount of additional tooling was required in the fabrication of P–39 airplanes. In connection with the plaintiff's quotations on each of the fixed-price contracts, except the last two British contracts, the plaintiff submitted a breakdown of its estimated costs of production. These cost estimates contained no provision for the amortization of any part of the deferred experimental, development and production tooling costs.

A substantial portion of the experimental expense and production tooling costs had not been determined or set up in the deferred account at the times the plaintiff submitted its estimates of production costs for fixed-price contracts which it received during 1939 and 1940.

The plaintiff's estimated tool charges for the various fixed-price contracts, other than the deferred costs, totaled $2,597,435.40. Its actual tooling costs for fixed-price production, other than the deferred tooling, were $2,233,239.47.

59 Some of the tools which had been provided as a preliminary to production and deferred for allocation against future production, would become worn out by use or obsolete as a result of current changes in design. Some were reworked and others were scrapped and replaced. The costs of reworking or replacing original tooling would be charged against current production and would be included in the tool costs in the preceding paragraph.

AMORTIZATION OF EXPERIMENTAL, DEVELOPMENT AND PRODUCTION TOOLING EXPENSE

12. As of December 31, 1940, the plaintiff had capitalized and deferred experimental, development and production tooling expense, as follows:

	Amounts expended and deferred by plaintiff	Disallowed by Army Audit	Net amounts subject to amortization
Experimental and development expense (Finding 6)	$1,528,760.66	$29,021.43	$1,499,739.23
Production tooling for P-39's (Finding 10)	1,894,109.57	19,383.80	1,874,725.77
Total	3,422,870.23	48,405.23	3,374,465.00

13. The plaintiff originally planned to amortize its deferred costs of $3,374,464 or the basis of the number of planes delivered and to be delivered on all contracts on hand at the end of each year, and by prorating such costs annually against deliveries made during the current year.

A copy of the memorandum by Paul C. Gillette, Engineer Revenue Agent, dated March 12, 1942, in reference to the plaintiff's operations for the years 1939 and 1940, was furnished to the plaintiff. It contains the following recommendation:

> That the entire costs at December 31, 1940, in the Development and Jig Expense Account, including the losses incurred, not charged off in prior years, on the Airacuda and Airabonita models, be amortized at a rate represented by the ratio of planes produced during the year compared with the total of planes produced and on order at the end of the year.

This recommendation was in harmony with the plaintiff's original plan of amortization.

60 Under the aforesaid plan the amount of amortization applicable to each airplane produced and delivered would decrease from year to year in proportion to the total increase in the number of planes under contract at the end of each year. At the end of the year 1940, the plaintiff had contracted to deliver approximately 1600 airplanes under its fixed-price contracts.

14. During 1941, the plaintiff received an additional fixed-price contract W 535 ac–32 for 180 planes and equivalent in parts. This contract appears in the table of fixed-price contracts, Finding 9. In the latter part of the same year, the plaintiff entered into two cost-plus-fixed-fee contracts for 2,392 airplanes of a similar type. The plaintiff's officials were not certain that its amortization costs

would be approved for reimbursement under its CPFF contracts, and avoided any question of allowable reimbursements by limiting its amortization of the deferred charges to the fixed-price contracts only. The plaintiff added only the additional planes covered by the fixed-price contract entered into in 1941, and the amounts charged to each plane thereafter remained constant.

15. The plaintiff's annual reports which were prepared and certified to by Price, Waterhouse & Company, certified public accountants, contain the following explanatory comments regarding the treatment of experimental, development and production tooling costs:

ANNUAL REPORT FOR 1938

The company, from its inception, has charged currently to costs of contracts in progress all experimental and development work as the contracts were completed. During the year 1938 substantial experimental and development work of basic future value to the company was accomplished in connection with a contract for the design and construction of an experimental airplane. The total expenditures, including the costs for basic development above referred to, charged to the costs of such contract, plus the estimated costs to complete, amounted to $128,052.77 over and above the contract price of the experimental plane. The sum of $128,052.77 was transferred to a deferred account at December 31, 1938.

61 ANNUAL REPORT FOR 1939

C—The deferred experimental and development expenses were in respect of two experimental airplanes.

The first of these (known as the Airacuda) was practically completed at December 31, 1937, and the estimated excess of its cost over the contract sales price was charged to profit and loss accounts for the year 1937. Subsequent to the delivery of the airplane in 1938 expenditures were made in connection with improvements in design and in further development of this project. Such additional expenditures, amounting to $200,320.23 have been deferred at December 31, 1939, as, in the opinion of the management, the development of this type of airplane has a probable value to the Company in connection with expected future sales. A contract for 13 Airacudas for service test involving three experimental variations of the original Airacuda, now in progress, is expected to be completed during 1940. Since the date of closing the annual accounts the Company has made substantial expenditures, not theretofore anticipated, in connection with the contract for thirteen

Airacudas. The amount of the total excess costs over the contract price has not been determined at this time.

The second of the experimental airplanes is being constructed for the Navy and the amount of $217,682.92 deferred in respect to this airplane is the excess of the estimated total cost when completed over the contract sales price. In the opinion of the management, such excess costs constitute development and experimental expenditures of value in connection with expected orders for this or similar types of aircraft.

The amount of $128,052.77 deferred at December 31, 1938, in respect of another experimental airplane has now been transferred to costs of airplanes of similar type for which contracts were received in 1939; accordingly the amount deferred at December 31, 1938, is included in the inventory of work in progress at December 31, 1939.

It is the Company's intention to charge the deferred experimental and development expenses to costs of future production (exclusive of the service test order above referred to) or, if and when the projects are abandoned, to charge them off to profit and loss accounts.

ANNUAL REPORT FOR 1940

During the past five years, the Company has developed three types of Airplanes known as Airacobra, Airacuda, and Airabonita, all three incorporating certain similar basic new de-
62 velopments. In the opinion of the management the excess costs on experimental and service test contracts constitute experimental and development charges and, together with costs of tooling for production, have been deferred. Such costs amounted, in the aggregate, to $3,422,870.23 at December 31, 1940 and consisted of charges on the Airacobra of $2,123,195.87, on the Airacuda of $889,499.48 and on the Airabonita of $410,174.88. The Company is at present concentrating on the manufacture of Airacobras, and it is the Company's intention to absorb the aggregate of the foregoing charges on the basis of the quantities of this model under contract. Amortization amounting to $70,773.45 has been charged against cost of goods sold in 1940.

ANNUAL REPORT FOR 1941

Experimental, development and production tooling expenditures amounting to $3,352,096.78 were deferred at December 31, 1940, to be absorbed on the basis of certain quantities of aircraft under contract. Of this amount an amortization of

$1,998,184.02 applicable to aircraft delivered during 1941 was charged to cost of goods sold for that year.

During 1942, the plaintiff amortized the remaining experimental, development and production tooling costs in its deferred account against deliveries of airplanes under its fixed-price contracts.

16. Thus at the end of 1942, the plaintiff had amortized its entire deferred costs for experimental, development and production tooling against deliveries under its fixed-price contracts, as follows:

Contract number	1940	1941	1942	Totals
United States				
W 535 ac-12635	$27,880.45	$ 1,923.18	.....	$ 29,803.63
W 535 ac-13383	42,893.00	128,853.06	.....	171,746.06
W 535 ac-15675	.....	934,665.48	$ 382,712.82	1,317,378.30
W 535 ac-32	.....	.....	346,172.40	346,172.40
Totals	70,773.45	1,065,441.72	728,885.22	1,865,100.39
British				
A-218	.....	369,250.56	15,385.44	384,636.00
A-1326	.....	405,790.98	75,004.02	480,795.00
A-1476	.....	157,700.76	534,638.08	692,338.84
Totals	.....	932,742.30	625,027.54	1,557,769.84
Totals	70,773.45	1,998,184.02	1,353,912.76	3,422,870.23

63 COST-PLUS-FIXED-FEE CONTRACTS

17. In the meantime, commencing August 14, 1941, the plaintiff had entered into a series of cost-plus-fixed-fee, or CPFF, contracts with the defendant through the United States Army Air Corps for the production of P–39 or Airacobra airplanes.

Under the CPFF contracts the defendant agreed to reimburse the plaintiff for the cost of manufacturing and in addition to pay the plaintiff a fixed fee as provided in each of such contracts. The particular contracts, with dates of execution, are described in the following table:

Item	Date of contract	Contract numbers	Airplanes and equivalent in spare parts	Type	Estimated Costs	Fixed fee specified
(I).....	8/14/41	W 535 ac-20910	1,980	P-39D....	$70,960,740	$4,257,644.40
(J).....	9/10/41	DA W 535 ac-156 ..	412	P-39D-1 .	14,985,926	899,155.56
(K).....	6/29/42	W 535 ac-29318	2,700	P-39E ...	88,670,000	3,546,800.00
	4/13/43	Increase	2,470	P-63A-1 .	64,814,800	2,592,592.00
(L).....	9/28/43	W 535 ac-40071	2,600	P-39Q ...	68,387,200	2,735,488.00
Totals.....	.....	.....	10,162	.....	307,818,666	14,031,679.96

By supplemental agreement dated September 29, 1942, contract W 535 ac–29318 was changed to provide for deliveries of Model P–63A–1 in lieu of the P–39 type specified under the original contract. Contract W 535 ac–40041, dated January 5, 1944, for 2,470 planes and equivalent in spare parts, type P–63A–1, was combined on April 13, 1945, and made a part of contract W 535 ac–29318 and is represented by the increase as noted in the above table.

The production of P39 models was discontinued in April 1944 on all of the above-described contracts and changed over to P–63 models on which production was thereafter continued.

Deliveries were completed under contract DA W 535 ac–156, W 535 ac–40071 was terminated November 3, 1944, and contracts W 535 ac-20910 and W 535 ac-29318 were terminated for the convenience of the Government August 14, 1945. Termination settlement agreements were consummated pursuant to the Contract Settlement Act of 1944.

64 The foregoing contracts are filed as Exhibits I, J, K, and L, respectively, with Plaintiff's Exhibit 1 (the stipulation of facts) and are made a part hereof by reference.

18. Each of the CPFF contracts contains the following provisions:

ARTICLE 3. CONSIDERATION

* * * * *

(b) For the purpose of determining the amount payable under this Contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T.D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

(1) All costs which have been incurred by the Contractor in anticipation of this Contract and prior to the signing thereof, and which if incurred after the signing of this Contract, would have been considered as allowable items of cost within the meaning of said Regulations, shall be considered as allowable items of cost incurred hereunder.

Article 3 (b) (2) of contracts W 535 ac–20910 and DA W 535 ac-156, and Article 3 (d) of contracts W 535 ac-29318 and W 535 ac-40071 provide:

(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of

cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this Contract, notwithstanding any provisions contained in the specifications or other documents incorporated in this Contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense or without cost to the Government.

Section 26.9 of Chapter 1 of Title 26, Code of Federal Regulations, as contained in T. D. 5000, is a promulgation of regulations governing the computation of Excess Profits Taxes, and provides, in part, as follows:

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of
65 manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

Said Section 26.9 of T. D. 5000 further provides in subparagraph (g) (4) thereof as follows:

• • • Among the items which shall not be included as a part of the cost of performing a contract or subcontract or consid-

ered in determining such cost, are the following: * * * losses on the other contracts; * * *

19. CPFF contracts W 535 ac-20910, DA W 535 ac-156, and W 535 ac–29318, provide in Articles 16 and 17 (a) thereof, as follows:

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon
66 the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

ARTICLE 17. DEFINITIONS

(a) The term "head of the department" as used herein shall mean the head or any assistant head of the executive department or independent establishment involved, and the term "his duly authorized representative" shall mean any person authorized to act for him other than the Contracting Officer.

CPFF contract W 535 ac–40071 provides in Article 16 thereof, as follows:

ARTICLE 16. DISPUTES

Except as otherwise specficially provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. * * * Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

REALLOCATION OF DEFERRED COSTS TO ALL PRODUCTION CONTRACTS

20. In 1942, at which time the plaintiff was engaged in production on CPFF contracts described in Finding 17, the Internal Revenue Bureau of the Treasury Department required that, for income tax purposes, the experimental, development and production
67 tooling expenses should be allocated to airplanes produced under CPFF contracts as well as the fixed-price contracts. The Plaintiff declined to accept this ruling and continued to amortize the remaining deferred charges for experimental, development and production tooling costs against the deliveries of airplanes under its fixed-price contracts during the remaining months of 1942, as set forth in Finding 16. The Bureau of Internal Revenue, however, adjusted the plaintiff's income for 1941 and 1942 for amortization by allocating such costs to deliveries under fixed-price contracts and deliveries made and to be made under CPFF contracts. Additional taxes assessed and paid for 1941 and 1942 totaled approximately $1,337,474.89.

21. On September 19, 1942, Charles L. Beard, then Secretary and Treasurer of the plaintiff corporation, in a memorandum directed to John Berry, Jr., Comptroller of the plaintiff corporation, made *inter alia* the following statement of policy in connection with such deferred experimental, development and production tooling expenses as it related to the above-mentioned suggestion then being made by the Bureau of Internal Revenue:

> This item should be allowed as an amortization expense against the fixed price contracts only in view of the fact that any amortization to be allowable under a cost-plus-fixed-fee contract would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost plus contracts in view of the position taken by the Government that prior to our entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses.

On April 2, 1943, John Berry, Jr., prepared and submitted to the Resident Auditor, Army Air Forces, a "Statement of Accounting Policies, Pertinent to Operations Under Cost-Plus-A-Fixed-Fee Supply Contracts," in which he made the following statement in connection with deferred charges for experimental, development and production tooling expenses:

> 3. Deferred charges.—
>
> • • • • •
>
> (c) Experimental, development and production tooling ex-
> 68 penses are written off against the deliveries of the items to

which expenditures apply. No experimental expense is charged to overhead applicable to CPFF contracts. • • •

22. On September 7, 1943, the plaintiff wrote to the Price Adjustment Board, War Department, New York City, an outline of its proposed future amortization of said deferred charges. Major Knox B. Phagan was at that time Army Air Corps Price Adjustment Officer. Said letter is as follows:

Pursuant to our telephone conversation this afternoon, we should be glad if you would indicate your approval of the method to be followed in amortizing development and experimental expenses and production tooling costs of P–39 airplanes.

Our records as of December 31, 1942, and the schedules originally submitted to you showed that we had amortized the full amount of these costs against fixed price contracts. You objected to such treatment on the ground that the costs should be amortized over cost plus a fixed fee as well as fixed price contracts. The Bureau of Internal Revenue in examining our Federal income and excess profits tax return for the calendar year 1941 had made the same objection and required us to amortize the costs over all airplane contracts then held by us. In view of the position taken by the Bureau of Internal Revenue and yourselves we have agreed to amortize the experimental and development expenditurs over all contracts for P-39 and P-63 airplanes and the P-39 production tooling expenditures over all contracts for P–39 airplanes, provided that the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office.

Under date of August 14, 1943 we provided you with two schedules which set forth in detail the amounts and contracts involved in the write-off from January 1, 1940, to June 30, 1943, on an actual write-off basis and through the balance of 1943 and 1944 on an estimated basis.

The method agreed upon involved a determination of each of the two amounts involved, which amounts are as shown by our books (and less adjustments aggregating $2,892.19 are as shown by a report of an Agent of the Bureau of Internal Revenue as of December 31, 1940) less adjustments made by the
69 Contract Audit Section of the Army Air Forces as a result of their examination of the costs. The amounts are as follows:

	Development and experimental	P-39 production tooling	Together
Costs to December 31, 1940 (there were no additions subsequently)	$1,528,760.66	$1,894,109.57	$3,422,870.23
Less—Costs disallowed by Contract Audit Section, Army Air Forces	29,021.43	19,383.80	48,405.23
Amount to be amortized as agreed upon with Price Adjustment Board and Contract Audit Section, Army Air Forces	1,499,739.23	1,874,725.77	3,374,465.00

The last amounts shown above are to be amortized over all fixed price and cost plus a fixed fee supply contracts for P-39 and P–63 airplanes as follows:

The sum of the number of airplanes and equivalents on order and undelivered at the beginning of the year and the number of airplanes and equivalents ordered during the calendar year is to be divided into the unamortized cost as of the beginning of the year, the resulting quotient represents the amortization per airplane. The amortization per airplane multiplied by the number of airplanes and equivalents accepted by the Army Air Forces during the period for each contract results in the amortization per contract.

We believe the foregoing sets forth the understanding between us as to the amortization of the expenditures for experimental and development and P–39 production tooling and if it is in accordance with your understanding we should like you to so indicate by signing one copy of this letter and returning it to us.

Yours very truly,

BELL AIRCRAFT CORPORATION,
(Signed) JOHN BERRY, JR.,
Comptroller.

The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

(Signed) KNOX B. PHAGAN,
Maj. A. C., Price Adj. Officer.

Date: Sept. 9, '43.

The plan of amortization outlined in the above letter is in accordance with the decision of the Internal Revenue Bureau. It was the plaintiff's original plan of amortizing these costs
70 against production under fixed-price contracts before it had

received any of its CPFF contracts. Major Phagan was then Chief of the Price Adjustment Section, Eastern District, Air Forces.

23. On September 9, 1943, the plaintiff's comptroller issued instructions for the restoration to the deferred account the proportion of experimental, development and production tooling which became applicable to airplanes delivered and to be delivered under the CPFF contracts, in accordance with the approved plan of reamortization. There was restored the sum of $2,286,819.95, consisting of:

Experimental and development costs	$1,035,918.73
Production tooling for P-39 planes	1,250,901.22

The unrestored difference of $1,087,645.05 previously amortized represented that portion of experimental, development and production tooling which was applicable to deliveries under the fixed-price contracts in accordance with the approved plan of reamortization.

Reimbursement vouchers were prepared by the plaintiff and submitted in the sum of $451,179.96 for reallocation of amortization of experimental, development, and production tooling on deliveries under CPFF contracts during 1942 and $848,676.06 for deliveries under CPFF contracts during January to August, inclusive, of 1943, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$370,552.30	$819,571.64	$1,190,123.94
DA W 535 ac-156	37,318.96	72,413.12	109,732.08
Total	407,871.26	891,984.76	1,299,856.02

The defendant's Contracting Officer approved the above vouchers for reimbursement under the CPFF contracts, and the plaintiff was paid the said sums by the defendant's Finance Officer.

24. Commencing in October 1943, the plaintiff submitted additional reimbursement vouchers for experimental, development, and tooling costs, representing the proportionate
71 amounts applicable to deliveries subsequent to August 1943 under CPFF contracts, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$194,947.81	$ 79,991.20	$274,939.01
DA W 535 ac-156	13,888.85	4,371.50	18,260.35
W 535 ac-29318	223,288.09	69,895.04	293,183.13
W 535 ac-40071	195,922.72	204,658.72	400,581.44
Total	$628,047.47	$358,916.46	$986,963.93

The above sums represent vouchers for all of the remaining experimental, development, and production tooling costs for which the plaintiff claimed reimbursement. No part of these sums has been paid.

25. As these vouchers began to arrive for audit in October 1943 the defendant's Resident Auditor, Roland Campbell, had been replaced by Frank Ferris. About the same time, Bancroft Mitchell, the Contracting Officer for the plaintiff's CPFF contracts, was replaced by Maj. Harold B. Davies, who acted both as Administrative Contracting Officer and Termination Contracting Officer.

The Assistant to the Resident Auditor, James D. DiLapo, recommended against approval of these vouchers for reimbursement on the ground that the plaintiff had consistently charged its experimental, development and production tooling costs against deliveries under its fixed-price contracts, and for the further reason that DiLapo considered such costs as losses on other fixed-price experimental contracts which would not be reimbursable costs under CPFF contracts. Approval of these vouchers was withheld by Ferris.

In February 1944, the defendant's Resident Auditor Ferris was replaced by one Harry Liebman, who likewise withheld approval of these vouchers on the ground that the CPFF contracts contained no provision for payment of experimental, development and production tooling expenses, except by reference to T. D. 5000, and for the further reason that the plaintiff had previously amortized such costs against fixed-price contracts.

Major Davies declined to approved these vouchers, since these deferred costs had been previously amortized against
72 deliveries under fixed-price contracts, and he thought the plaintiff had changed its method for the reamortization of such costs over all contracts as a result of the decision of the Bureau of Internal Revenue, but without the approval of the Contracting Officer. By his decision of March 1, 1945, the Contracting Officer denied the plaintiff's claim for reimbursement of these vouchers.

26. In April and May 1944, the Chief Cost Auditor for the General Accounting Office, Buffalo area, submitted to the Resident Auditor a series of "informal inquiries" in respect to the reimbursements of experimental, development and production tooling costs by Col. J. Harris, Finance Officer, in August and September 1943, summarized in Finding 23, as follows:

		Reimbursement exceptions	
Informal inquiry	Dated	Contract	Total payments
777	4/25/44	W 535 ac-20910	$1,064,888.18
778	4/25/44	DA W 535 ac-156	109,732.08
789	5/13/44	W 535 ac-20910	125,235.76
Total (Finding 23)			$1,299,856.02

Each of the foregoing inquiries made exception to such payments as follows:

> Since the entire amount of the Deferred Experimental and Development Expenses and the Production Tool Expenses were amortized or written off against prior commercial and Government fixed price contracts by the contractor, the status of the account at the time of the negotiations with respect to the estimated costs under his contract was such as to preclude consideration thereof as an existing "Deferred" or "unliquidated" charge to the contract and the fact that for tax purposes the account was reopened and amortized in part against this contract would appear to afford no proper basis for considering the amount so amortized as a reimbursable item of cost under this contract.

27. By letters dated June 29, 1944, the Resident Auditor, Harry Leibman, advised the Chief Cost Auditor for the General Accounting Office at Buffalo that deductions were made on vouch-
73 ers listed in the said letters to recover payments for experimental, development and production tooling costs, in accordance with informal inquiries 777, 778 and 789. Copies of these letters were furnished the plaintiff.

The Contracting Officer held up the vouchers on which the Resident Auditor made deductions, and took no action upon them until September 1944.

In the interim the Comptroller General of the United States issued formal notices of exception and suspensions of the accounts of Colonel J. Harris, Finance Officer at Buffalo, dated August 18, 1944. These notices covered the sums of $1,064,888.18 and $109,732.08, on which exceptions were noted by informal inquiries Nos. 777 and 778 and for the same reason. They were received by the Finance Officer August 21, 1944. Recoupment of these sums was made immediately by the Finance Officer on vouchers for monies otherwise due the plaintiff, and the Comptroller General was advised thereof by reply endorsements August 25, 1944.

On September 6 and 8, 1944, the Contracting Officer transmitted to the Finance Officer for settlement, groups of the plaintiff's vouchers, which included the vouchers on which deductions were made by

the Resident Auditor, as above. The Contracting Officer reinstated vouchers for $1,064,888.18 and $109,732.08 for which sums had been recovered by the Finance Officer, but other deductions for $125,235.76 were approved by him in compliance with informal inquiry and exception No. 789, and in harmony with the formal notices of exception and suspension previously received by the Finance Officer.

On September 12, 1944, the Finance Officer received a formal notice of suspension from the Comptroller General dated September 11th for the sum of $125,235.76, in accordance with informal inquiry No. 789. A reply endorsement was issued the following day by the Finance Officer for removal of the suspension since this sum had been deducted from vouchers for amounts otherwise due the plaintiff. Thus the payments totaling $1,299,856.02 for experimental, development and production tooling costs reimbursed to the plaintiff on CPFF contracts were fully recovered by the defendant.

74 28. Experimental, development, and production tooling costs which were amortized and vouchered for reimbursement by the plaintiff under CPFF contracts, Findings 23 and 24, are combined as follows:

Contract number	Experimental and development expense	Production tooling costs	Total
W 535 ac–20910	$ 565,500.11	$ 899,562.84	$1,465,062.95
DA W 535 ac–156	51,207.81	76,784.62	127,992.43
W 535 ac–29318	223,288.09	69,895.04	293,183.13
W 535 ac–40071	195,922.72	204,658.72	400,581.44
Total	$1,035,918.73	$1,250,901.22	$2,286,819.95

29. The Contracting Officer declined to approve the additional vouchers for $986,963.93 (Findings 24 and 25), and on March 1, 1945, issued his decision denying any reimbursement. This decision states in part:

> It appears that the said sum of $2,286,819.95 which Bell has charged on its books against CPFF contracts does not, in fact, represent costs of performing such CPFF contracts and that reimbursement for such costs under the said CPFF contracts would result in Bell's receiving double payment from the Government therefor.

The sum of $2,286,819.95 represents the $1,299,856.02 which had been approved by the predecessor Contracting Officer, paid, and recouped by the Finance Officer under suspension by the Comptroller General, as well as the unpaid vouchers totaling $986,963.93, summarized in Finding 24, for which no payment had been made.

30. On March 27, 1945, the plaintiff made timely appeal from the findings and decision of the Contracting Officer, in denying payment on vouchers totaling $986,963.93. The sum of $1,299,856.02, which had been previously reimbursed and was noted for exception and suspension of the accounts of the Finance Officer by the Comptroller General, was not appealed by the plaintiff nor considered by the War Department Board of Contract Appeals, representing the Secretary of War.

On April 29, 1946, the War Department Board of Contract Appeals rendered its decision on the plaintiff's appeal in
75 which it denied the reimbursement of the said sum of $986,963.93. This decision states in part:

> The experimental and development costs are clearly within the category of indirect costs as defined by T. D. 5000 and are specifically covered by Section 26.9 (d) of T. D. 5000—set out above. There is no specific reference in T. D. 5000 to the amortization of production tooling costs and appellant has not pointed out a specific provision of T. D. 5000 which it considers as providing for the allowance of such an item of cost. In the pamphlet issued by the War and Navy Departments entitled "Explanation of Principles for Determination of Costs Under Government Contracts" (Par. 18), it is indicated that items such as royalties and the amortization of the initial cost of dies, patterns, and special tools can logically be classified as direct shop costs and be charged to contracts on an equitable basis of apportionment. Section 26.9 (c) (5) (D of T. D. 5000 set out above also provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. It is clear from the record and evidence that the production tooling was used in the performance of CPFF contracts calling for the production of the P–39 type of airplane. It would seem, therefore, that items of this type are within the intent and meaning of T. D. 5000.
>
> • • • • •
>
> Although it is true that costs of this type may properly be allowed as reimbursable items under T. D. 5000, it does not follow that such costs must be reimbursed under T. D. 5000 in all cases and under all circumstances. In order to determine whether such items of costs should be reimbursed it is necessary to examine all of the circumstances and facts involved. The subject costs—both engineering and development, and production tooling costs—were incurred a considerable time before any of the CPFF contracts were entered into. The production tooling costs were incurred for the express and admitted purpose of performing certain fixed-price contracts then on hand

or in process of negotiation. They were not incurred in anticipation of the CPFF contracts and would have necessarily been incurred regardless of whether any further contracts for the P–39 type of airplane were received or not. The engineering and development costs were incurred during the period 1938 to 1940 and the costs were capitalized because it was
76 felt that the development in connection with which they were incurred had a probable value in connection with expected future sales. In 1940 appellant entered upon a course of conduct by which these costs were charged against certain fixed-price contracts. The procedure of charging these costs against fixed-price contracts was continued during 1941 and 1942 in accordance with the mentioned plan to the effect that at the end of 1942 all of the costs in question had been absorbed. During this period some of the subject CPFF contracts were entered into and all of them were negotiated prior to August of 1943 at which time appellant changed its plan of amortization to the one now contended for. It is clear from the record that no portion of these costs was included in the estimates under the CPFF contracts and no specific consideration was given to the question of reimbursement in the negotiation of the subject contracts. It also may be reasonably concluded that appellant had no intention, at the time the contracts were entered into, of seeking reimbursement for such costs since its accounting method did not contemplate reimbursement.

• • • • •

For the reasons herein set out the appeal insofar as it relates to contracts numbered W 535–ac–20910, W 535–ac–29318, W 535–ac–40071, and W 535–ac–40041 is denied.

In respect to contract DA W 535 ac–156, the President of the Board, the duly authorized representative of the Secretary of War, decided in accordance with the entire Board on other contracts, and denied the plaintiff's appeal insofar as it related to this contract.

The plaintiff's application for a rehearing was denied by the Board May 31, 1946.

This decision is in evidence as Exhibit P to the stipulation (Plaintiff's Exhibit 1) and is incorporated herein by reference.

31. As heretofore related (Finding 17) all of the CPFF contracts were terminated for the convenience of the Government upon termination of hostilities. Termination settlement agreements were entered into pursuant to the Contract Settlement Act of 1944, in which the plaintiff made reservations in respect to its claims for reimbursements under the CPFF contracts, as follows:

The Supplemental Settlement Agreement dated December 21, 1945, covering the termination of contract W 535 ac-
77 20910, contains the following reservation in Article 4 (c) (2) (b):

> Claim for experimental and development and research costs in the amount of $1,465,062.95 which is now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated May 15, 1946, covering the termination of contract W 535 ac–29318, contains the following reservation in Article 4 (c) (2) (b):

> $293,183.13 of experimental and development expenses now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated February 22, 1946, covering the termination of contract W 535 ac–40071, contains the following reservation in Article 4 (c) (2):

> Claim by the Contractor against the Government, as to which his right of reimbursement is disputed, which is excluded without prejudice to the rights of either party, to wit, claim for experimental and development and research costs in the amount of $400,581.44, which is now the subject of an appeal pending before the War Department Board of Contract Appeals.

These termination settlement agreements are attached to the respective contracts to which they pertain, as Exhibits I, K, and L to the stipulation filed and are incorporated herein by reference.

At the time the settlement agreement was consummated for contract W 535 ac–20910, there was pending before the War Department Board of Contract Appeals the plaintiff's claim for reimbursement of costs for $274,939.01. The difference of $1,190,123.94 had been reimbursed to the plaintiff, but was recouped by the Finance Officer upon notice of exceptions and suspension by the Comptroller General.

32. On March 27, 1945, the plaintiff executed a renegotiation agreement pursuant to Section 403 of the Sixth Supplemental National Defense Appropriation Act, 1942, as amended, in respect to excessive profits for its fiscal year ending December 31, 1942. This agreement was signed by Colonel Maurice Hirsch, G. S. C., for all services of the United States concerned, and was approved for the Under Secretary of War May 22, 1945. The said agree-

78 ment is in evidence as stipulation Exhibit N, attached to the Plaintiff's Exhibit 1, and is incorporated herein by reference. The said agreement covered profits for 1942 on both fixed-price contracts and CPFF contracts with the United States. It provided for refund by the plaintiff of $7,714,000 of excessive profits for the year 1942, after first applying the tax credit applicable to such profits. This agreement provides in part: (See also Finding 16 herein.)

EXHIBIT "C"

• • • • •

PRINCIPLES UNDERLYING SEGREGATION OF SALES AND PROFITS

• • • • •

Allcation of Cost of Sales and Expenses

1. *Cost of sales:*

• • • • •

(g) Deferred Experimental Development, and Production Tooling Expenses in the amount of 1,353,913 were amortized over all planes delivered under Fixed Price Contracts during the year. For the purpose of computing the additional refund under Paragraph VIII of the Agreement, the adjusted amortization chargeable to 1942 of 638,683 was allocated on the basis of the total number of planes delivered under all contracts, both Fixed Price and CPFF.

• • • • •

VIII. In arriving at the refund herein the items of Deferred Experimental Develpoment, and Production Tooling Expenses in the amount of $728,885.22 have been charged as Costs against Renegotiable Fixed Price Contracts for said fiscal year. The Contractor, in order to conform its method of handling these items to the method adopted by the Bureau of Internal Revenue, has adjusted its figures for said fiscal year by amortizing these items over the total number of planes of the Airacobra type produced, or to be produced, on both Fixed Price and CPFF Contracts (Production Tooling limited to P–39 Models). Such method of amortization and the corresponding reallocation of costs to CPFF Contracts, as well as Fixed Price Contracts, has been tentatively approved by the Army Air Forces, and if the amount allocated to the CPFF Contracts is finally approved by both the Army Air Forces and the General Accounting Office of the Comptroller General of the United States, and reimbursement therefor, is made,
79 the Contractor agrees to pay to the United States as an ad-

ditional refund the sum of $667,000, on account of which the Contractor shall receive credit for Federal Income and Excess Profits Taxes thereon as determined by the Bureau of Internal Revenue as provided in Paragraph VII hereof.

33. The amortization allowance of experimental, development and production tooling to fixed-price contracts only under the foregoing settlement agreement was contrary to the allocations by the Bureau of Internal Revenue, which amortized these costs upon production for all contracts.

As a result of a plan applied by the Bureau of Internal Revenue, additional assessments were made against the plaintiff's income for 1941 and 1942 in the approximate sum of $1,337,474.89. By deducting amortization which it allocated to production under CPFF contracts, assessments were reduced for the years 1943, 1944 and 1945 by the approximate sum of $1,305,418.72. The net increase in tax assessments was approximately $32,056.17.

The amortization by the Bureau of Internal Revenue was applied as a deduction against the plaintiff's net income from the fixed fees under CPFF contracts, whereas, the plaintiff claims that no reduction should have been made to its fixed fees on account of amortization, but that the full sum of $2,286,819.95 should have been reimbursed as a portion of its costs of performing these contracts.

VALUE OF EXPERIMENTAL AND DEVELOPMENT WORK TO COST-PLUS-FIXED-FEE CONTRACTS

34. Experimental and development costs capitalized and deferred by the plaintiff for allocation to future production were not segregated as between specific experimental contracts to which they might apply. It was impossible to make any reasonably correct segregation of such costs, since the improvements in design and fabrication developed in the earlier operations were carried forward and applied on later experimental and development work, and finally into production contracts. These costs represent deferred values of designing and experience in fabrication rather than costs of any particular airplane contract.

The plaintiff took over the plant on Elmwood Avenue, Buffalo, New York, in the fall of 1935, which had been
80 vacated by Consolidated Aircraft Company upon its transfer to California, and an abundance of experienced personnel who elected to remain in Buffalo.

The plaintiff's first work involved the installation of an Allison model engine in the nose of a Consolidated airplane. It was the first installation of this kind for the Allison model, which was a heavy 1,000 h. p. engine, whereas other models previously used were

normally about 600 h. p. models. It required investigation of the strength of the wings, tail, fuselage and landing gear. The plaintiff's next job was subcontract work for manufacturing all-metal, aluminum, riveted wings for Consolidated flying boats.

The first experimental plane was the XFM–1 Airacuda contracted for May 12, 1936. It was substantially completed by the end of 1937. All costs of experimental and development work on the above projects were charged against these contracts currently or to the plaintiff's profit and loss account, up to and including December 31, 1937. The plaintiff continued further development work on the XFM–1 model in 1938, and later on a contract for service test models of the same type.

35. Some of the basic principles of design and fabrication, which the plaintiff developed on experimental contract work and incorporated into the P-39 production models, include the following:

(a) The installation and successful operation of a liquid-cooled Allison engine, involving installation problems and other features of design necessary to operations.

(b) The extension of the drive shaft, so that the propellers could operate more distant from the engine.

This feature was designed on the XFM-1, where the engine was housed in the wing structure, and the pusher-type propellers operated from the rear of the wings. The extension drive shaft was adopted in the P-39, by locating the engine in the fuselage to the rear of the pilot, with the extended drive shaft projected beneath the pilot and operating the propeller in the nose of the aircraft, thereby providing vision for the pilot and permitting the projecting nose of the plane to better accommodate the front wheel of the tricycle landing gear.

81 (c) The design and successful installation of air intake ducts for cooling the engine and oil systems, known as "ducted radiator", whereby an intake opening was provided in the leading edge of the wing for admitting air at high velocity.

The air then expanded into larger internal ducts slowing down its velocity for cooling purposes. The overhead air scoop was subsequently incorporated in all P-39's and P-63 planes. The intake was provided on top of these planes, instead of the front edge of the wing, but serving the same purpose of obtaining a simple duct system of air intake to the carburetor of the engine.

(d) The development and installation of a successful anti-shimmy dampening device for the nose wheel of the tricycle landing gear.

The nose wheel of this type of gear was provided with a swivel stirrup to steer the plane on the ground. The nose-wheel shimmy or oscillation was inherent in this type of gear, as the plane would take the runway at high speed or over rough roads. The first successful development of the shimmy dampening device was in connection with the XP-39, although the basic characteristics in this device were developed by the plaintiff in connection with the development and installation of a shock-absorbing gun mount for the XFM-1 plane.

(e) The successful installation of a 37mm. repeating cannon in the XFM-1.

In the flexible gun mountings for the Airacudas the plaintiff devised means of holding and supporting the gun so that it could be properly aimed and provided for the recoil in this type mounting. In the P-39's it was installed in a fixed mounting, but other features of feeding and ejecting the heavy empty cartridges were retained. Provision was made for retaining in the plane the empty shells that were ejected from the cannon, to avoid fouling or damage to the plane when they were ejected. In lieu of clips, which required manual changing, the plaintiff devised an automatic feed belt to carry the shells into firing position.

(f) Flush riveting, which was developed in the earliest experimental planes, was carried into all later production.

A high-strength aluminum alloy was specified for the
82 XFM-1 fighter plane built by the plaintiff under its first experimental contract. In order to take advantage of the higher structural tensility of this material the plaintiff, by a process of heat treating, sunk the rivets approximately flush with the surface of the metal, which resulted in a smoother external surface in this type of fabrication.

(g) In the construction of the XFL-1 Airabonita, the plaintiff designed and provided very heavy-duty landing gear to accommodate, without undue hazard, the catapult, deck landing and arresting equipment. This tougher type of landing gear was subsequently provided for P-39 models using the tricycle landing gear.

In connection with the XFL-1 for the Navy, the plaintiff also developed a nose-over beam, which extended in the fuselage above and behind the pilot for his protection in case the plane turned over. This feature was also incorporated in the production models of P-39 Airacobras.

(h) Engineering standards which were prepared for experimental work, consisting of short-cut repeat operations, tables and curves of technical information.

Once computed, these standards could be applied thereafter without recalculations.

(i) The earlier Allison engines furnished the plaintiff attained their greatest power at sea level.

In order to give them more power at high altitudes, the plaintiff installed General Electric turbo superchargers which were operated from the engines. Later Allison engines incorporated features to provide power at high altitudes, which duplicated the external unit and voided its further use.

(j) The plaintiff also developed and provided compartments in the wing structure of the experimental planes for carrying additional fuel, known as integral fuel tanks.

There were designed to be liquid tight and were enclosed by integral parts of the plane structure, such as the inside beams, bulkhead and outside sheeting. This feature was installed in P-39 models but it was not satisfactorily perfected because of difficulty with leakage, and was later superseded with bullet-proof storage tanks, by fitting the compartments with rubber and composition cells that would self seal any bullet penetration.

83 With the exception of the last two features above, the developments, engineering standards and fabricating processes acquired during the manufacture of experimental airplanes were incorporated and utilized on all production. The measure of value to production after 1940 is represented by the plaintiff's excess of costs on experimental airplanes over and above its recoveries under these contracts in the net amount of $1,499,739.23.

36. The plaintiff obtained a basic patent on its development of a hydraulic shimmy-dampening device in the steering mechanism of the nose wheel of the tricycle landing gear, and certain other patents for semi-automatic counter sinkers, twisted spar mills, routers and stake drills. It recovered substantial royalty payments for use of these devices by another manufacturer. As a result of proceedings before a Royalty Adjustment Board, the plaintiff was required to pay over to the Government some $691,666.24, under an indemnity agreement with the War and Navy Departments, representing all royalties collected by it.

There was included in the sums paid over one amount of $102,050.28, which the plaintiff had previously taken into its income and paid taxes thereon. The tax rate during the war years averaged approximately 70 percent of the plaintiff's total net income. No part of the royalties collected was retained by the plaintiff.

The Government also received credit of $360,000 on a contract for an improved model of the P-39, pursuant to an agreement with

the plaintiff dated April 11, 1940, which authorized the plaintiff to make certain deliveries to the British of the P-39 model airplanes in advance of deliveries under one of the production contracts for the Army Air Corps.

37. A fair measure of the value of experimental and development work applicable to all production contracts is to equalized profits realized by the plaintiff upon experimental and production fixed-price contracts.

After having amortized the total amount of experimental, development and production tooling expenses against its fixed-price production contracts, the plaintiff realized a net profit, before taxes and renegotiation of excess profits, of $18,280,732.50.

84 By adding back the experimental and development expense of $1,499,739.23, the profit would be $19,780,471.73, or 27.7 percent of the total value of $71,364,004.86 for these contracts.

The total value of experimental fixed-price contracts was $4,049,445. By applying the profit ratio of 27.7 percent, the plaintiff would have realized a profit of $1,121,696.27 on its experimental contracts. By adding to this sum the plaintiff's costs in excess of the prices realized on experimental contracts there is derived the sum of $2,621,435.50 for amortization over all contracts.

38. The plaintiff's net income on its fixed-price production contracts, after renegotiation and taxes, was approximately $4,637,607.63.

39. The sum of $1,499,739.23, which was capitalized and deferred by the plaintiff for allocation to future production, represented a fair and reasonable value of the general experimental and development work in benefits and savings on production contracts.

VALUE OF PRODUCTION TOOLING TO COST-PLUS-FIXED-FEE CONTRACTS

40. Production tooling for the P-39 model was provided during 1939 and 1940. At the end of 1940, the plaintiff capitalized and deferred for allocation to future operations, production tooling costs totaling $1,874,725.77.

This production tooling was used for the fabrication and assembly of airplanes under all of the fixed-price production contracts. Some of the tools other than assembly fixtures became worn out through use or became obsolete on account of current changes from time to time during production.

The major portion of tooling for the P-39 models was used throughout the production of this type of plane under the CPFF contracts. Where replacements or reworking of tools became nec-

essary, the costs were charged against current operations, so that when production under CPFF contracts was commenced the value of production tooling was substantially the same as when it was originally installed for use on fixed-price contracts.

In April 1944, the P-39 model was discontinued, and retooling became necessary for the production of P-63 models. All
85 tooling which could not be used in the production of the later model was scrapped and replaced upon approval of the defendant's plant clearance officer.

Lists of tools and equipment which could no longer be used on the new models were prepared by the plaintiff, and allocated to certain of the CPFF contracts then in process. The proceeds of the sale of these tools and fixtures were credited to the defendant on CPFF contracts.

The beneficial value of production tooling for P-39 model airplanes manufactured under CPFF contracts was at least equivalent to the beneficial use of such tooling to performance under the fixed-price production contracts.

41. In submitting bids for its fixed-price contracts the plaintiff also submitted data of estimated costs of performing these contracts, the details of which are appended to copies of these contracts. None of the estimates for performing the fixed-price contracts contain any provision for the amortization of experimental, development and production tooling costs.

Estimated costs in the cost-plus-fixed-fee contracts, as specified in Article 2 thereof, were based upon data on file in the office of the Chief of Air Corps, no details of which were attached to these contracts. There is no evidence that these data contained any estimate for the experimental, development and production tooling costs involved herein.

Article 3 (a) of the CPFF contracts provided for a fixed fee to the plaintiff of 6 percent of the estimated costs under the first two of these contracts and 4 percent of the estimated costs under the last two thereof. This Article contains the additional provision:

> • • • This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof; provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

The provisions for allowable costs are contained in the same article.

86 The plaintiff amortized its deferred costs for experimental, development and production tooling expense over all production contracts, as follows:

	Fixed-price contracts (Findings 12 and 23)	C P F F contracts (Finding 28)
Experimental and development expense....	$ 463,820.50	$1,035,918.73
Production tooling expense	623,824.55	1,250,901.22
	$1,087,645.05	$2,286,819.95

The amortization of $1,087,645.05 represents 1.52 percent of the total $71,364,004.86 value of fixed-price contracts, all of which were completed. The amortization of $2,286,819.95 on CPFF contract production represents .71 percent of the total estimated cost plus the fixed fees specified in these contracts. Deliveries called for under CPFF contracts were not completed and the contracts were terminated upon cessation of hostilities August 14, 1945.

The plaintiff's experimental, development and production tooling costs were properly deferred and included as an element of costs in performing its cost-plus-fixed-fee contracts. The amortization was applied in accordance with a reasonably consistent plan, ratably applied to the total number of P-39 model airplanes produced.

Respectfully submitted,

MARION T. BENNETT,
Commissioner.

87 ARGUMENT AND SUBMISSION OF CASE.

On January 11, 1951, the case was argued and submitted on merits by Mr. William M. Aiken for plaintiff; and by Mr. John B. Miller for defendant.

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89 *Special findings of fact, conclusion of law and opinion of the court by Howell, J. Dissenting opinion, in part, by Jones, Chief Judge. Dissenting opinion by Madden, J.*

BELL AIRCRAFT CORPORATION v. THE UNITED STATES

Mr. William M. Aiken for the plaintiff. *Messrs. Dudley, Stowe & Sawyer*, and *Messrs. Covington, Burling, Rublee, O'Brian & Shorb* were on the briefs.

Mr. John B. Miller, with whom was *Mr. Assistant Attorney General H. G. Morison,* for the defendant. *Mr. Thomas O. Fleming* was on the brief.

The Court, upon the evidence, the report of Commissioner Marion T. Bennett, and the briefs and argument of counsel, makes the following

SPECIAL FINDINGS OF FACT.

1. The plaintiff is a corporation organized and existing under the laws of the State of New York with its principal office and place of business in the Town of Wheatfield, Niagara County, New York.

2. The plaintiff was organized and commenced business in 1935, and thereafter, during all the times mentioned herein, the major part of the plaintiff's business has been the development and manufacture of military aircraft.

EXPERIMENTAL AND DEVELOPMENT COSTS DEFERRED

3. In 1936, 1937, and 1938, the plaintiff entered into certain experimental contracts with the defendant, through the United States Army Air Corps for the construction of certain
90 experimental and service test airplanes. Experimental airplanes were designated by the letter "X" preceding the model number, and the service test airplanes were designated by the letter "Y" preceding the model number. Other designations of type preceding the model number of particular airplanes hereinafter mentioned were "F" for "Fighter" and "P" for "Pursuit."

4. The following fixed-price experimental contracts were entered into between the plaintiff and the United States for fighter planes, in the performance of which the plaintiff incurred substantial expenditures over and above amounts received, which costs were set up on the plaintiff's books as deferred charges applicable to anticipated production:

Item	Date of contract	Contract numbers	Airplanes Units	Models	Designations	Contract price
(A)	5/12/36	W 535 ac-8773...	1	XFM-1	"Airacuda"	$ 390,300
(B)	9/27/37	W 535 ac-10341...	1	XP-39	"Airacobra"	245,880
(C)	4/20/38	W 535 ac-11122...	10	YFM-1	"Airacuda"	3,168,265
			3	YFM-1A		
(D)	11/8/38	63629	1	XFL-1	"Airabonita"	245,000
			16			$4,049,445

Contract No. 63629 was with the Navy, Bureau of Supplies and Accounts, and the others were with the Army Air Corps.

Articles 19, 21, 21, and 29, respectively, of the foregoing contracts provide for a nonexclusive, irrevocable right and license to the Government to use any and all discoveries, inventions, improvements and/or suggestions which are wholly or in part developed, perfected and/or reduced to practice with the aid and/or cooperation of the Government or of Government personnel, and/or by the contractor to meet explicit Governmental requirements or by the fulfillment of such contract.

Articles 26, 26 and 25, respectively, of the Army contracts provide:

> *Reproduction rights.*—It is understood and agreed that the contractor does not convey to the Government any reproduction rights in or to the articles and/or spare parts called for herein by virtue of the terms of this contract, except as hereinbefore set forth.

91 The plaintiff acquired a number of basic patents in connection with its development work, on which substantial royalties were realized.

5. All the airplanes delivered on these experimental contracts, as well as the production contracts received later, were powered by liquid-cooled Allison engines, furnished by the Government. The Government also furnished other materials and parts, consisting of the wheels, tires, tubes, propellors, guns, instruments and certain electrical and communications equipment.

The Airacuda was a twin-engine, five place. long-range fighter plane with pusher propellors operated by drive shafts to the engine. It was armed with two 37mm. repeating cannon, flexibly mounted in the nose of its engine nacelles, and two 50-calibre machine guns installed in the waist, with flexible mountings manually operated, with a wide sweep firing range upward, downward or rearward. These planes were originally designed with conventional landing gear, that is, with two wheels abreast, one under each wing and a tail wheel to carry the rear portion of the fuselage. The three YFM-1A service test model Airacudas incorporated the tricycle landing gear which had been developed in connection with the experimental Airacobra.

The Allison engines supplied for the experimental planes operated at maximum power at sea level. The plaintiff installed an external General Electric turbo supercharger, driven from the engine, which increased its power at high altitudes. Allison later delivered altitude-rated engines, which duplicated the external unit and voided its further use. Two of the service test Airacudas incorporated the altitude-rated engines. The Airacuda was approximately two and one-half times the weight of the Airacobra.

The Airacobra was a single-engine and propellor, single-seat, short-range interceptor fighter plane. The engine, mounted to the rear of the cockpit, operated the propellor at the nose of the plane by means of a drive shaft. A tricycle landing gear was developed in the experimental model which consisted of a retractable nose wheel and two retractable wing wheels. The Airacobra was armed with one 37mm. repeating cannon which fired through the shaft and hub of the propeller from a fixed mounting, and two
92 50-calibre machine guns which fired from fixed mountings between the propeller blades, so that the position of the plane governed the aim at a target, without any manual control.

The Airabonita was modeled after the Airacobra, but adapted to use on airplane carriers. The conventional landing gear was restored to this model and a tail hook was provided to engage the carrier deck arresting gear for landing purposes.

6. The first experimental Airacuda had been substantially completed by the end of 1937, and the excess of costs over the contract price for this unit was charged to profit and loss accounts for that year. Subsequent to the delivery of this airplane in 1938, the plaintiff incurred additional expenditures for the development and improvement in this design. The plaintiff's expenditures for the 13 test models of this design were also substantially in excess of the contract price received. These excess costs were capitalized as "deferred charges" in 1939 and 1940 for distribution as an element of cost against future production.

Much of the basic engineering and development designing in the Airacuda was carried forward and incorporated in the Airacobra which later entered quantity production for the Army Air Corps and the British Government.

The tooling for experimental contract work was of a temporary nature and fixtures for assembly were made of wood, very little of which had any useful value for later production. All excess costs on experimental contracts were classified as experimental and development expense. Such costs were accumulated from year to year during the performance of the several experimental contracts. No segregation of these costs was made as to their application to the specific contracts on which excessive costs were incurred, except the first amount deferred in 1938, which resulted from work on the experimental contract for the Airacobra.

The plaintiff deferred and capitalized as experimental and development costs the amount by which its total costs exceeded the experimental contract prices, as follows:

December 31, 1938	$ 128,052.77
December 31, 1939	511,776.21
December 31, 1940	888,931.68
Total	$1,528,760.66

93 Although the deferred experimental and development costs were not segregated in the plaintiff's accounts in respect to the specific contracts under which excess costs were incurred, the plaintiff's auditors arrived at an approximate allocation by deducting from the costs of fulfilling the contracts, the income received, as follows:

Airacudas	$ 889,499.48
Airacobra	229,086.30
Airabonita	410,174.88
Total	$1,528,760.66

The defendant's Army Audit Agency disallowed items totaling $29,021.43 (which disallowance is not involved in this dispute), leaving a balance of $1,499,739.23 in the deferred account for experimental and development expense, which sum represented the plaintiff's costs over and above the sums received under the contracts for experimental airplanes.

7. The plaintiff received no production contracts for any of the types described as Airacudas or the Airabonita airplanes. It received many contracts for great numbers of the Airacobra pursuit fighter plane, known as the P-39.

PRODUCTION TOOLING COSTS DEFERRED

8. April 26, 1939, the plaintiff entered into contract W 535 ac-12635 with the Army Air Corps for the delivery of 13 service test models of the Airacobra with additional parts at a fixed price of $1,073,445. Twelve of these planes were described as YP-39, Model 4-C, and one YP-39A, Model 4-D.

The work under this contract was merged in the shop with production on later contracts, and any additional experimental costs in connection with its performance were absorbed in the production costs on fixed-price production contracts.

Thereafter, from time to time, the plaintiff was awarded additional production contracts for P-39 Airacobras with both the United States and the British Governments. The earlier production contracts were fixed price, and the later ones were cost-plus-fixed-fee contracts. Under the cost-plus-fixed-fee contracts,
94 hereinafter referred to as CPFF contracts, the plaintiff was reimbursed for allowable costs of manufacture and was paid a fixed fee specified in the contract.

The production of P-39 Airacobras was continued on all of these contracts until April 1944, at which time the uncompleted contracts were amended to provide for deliveries of P-63 models. Numerous changes were made during the entire production period of the

P-39 models to reduce costs and facilitate production, to avoid field breakage and to improve functional operations.

9. The plaintiff received the following fixed-price contracts for the production and delivery of Airacobra fighter planes:

Item	Date of contract	Contract numbers	Unit planes and equivalent in spare parts	Models	Contract price
United States					
(E).....	4/26/39	W 535 ac-12635	13 1	YP-39 YP-39A	$1,073,445.00
(F).....	9/30/39	W 535 ac-13383	87	P-39C	2,833,236.00
(G).....	9/ 7/40	W 535 ac-15675 Increased	120 565	P-39D	4,962,220.00 21,276,912.79
(H).....	6/ 5/41	W 535 ac-32	180	P-39D-1	7,407,540.00
			966		$37,553,353.79
British					
	8/15/40	A-218	200	P-400	$9,517,507.55
	10/ 8/40	A-1326	250	P-400	9,647,163.33
	10/10/40	A-1476	360	P-400	14,645,980.19
Totals			810		$33,810,651.07
			1,776		$71,364,004.86

The United States contracts were entered into with the Army Air Corps.

The Model P-400 produced under British contracts was the British version of the P-39 and was of similar type and character as the Airacobra pursuit fighter planes specified under the contracts with the United States Army Air Corps.

The Army Air Corps contracts contain similar provisions, in respect to the right and license of the Government in any and all discoveries, inventions and improvements, as those set forth in Finding 4 for experimental contracts. These contracts also contain provisions substantially as follows:

95 *Provisions Reference Section 14 of the Act approved April 3, 1939—Limitation on Profits—It is expressly understood and agreed by both parties hereto that the contractor hereby agrees:*

• • • • •

(e) That the manufacturing spaces and books of its own plants, affiliates, and subdivisions shall at all times be subject to inspection and audit by any person designated by the Secretary of War, the Secretary of the Treasury and/or by a duly authorized committee of Congress.

• • • • •

Cost Records.—The contractor agrees to keep cost records in accordance with its own methods and practices of computing

costs of all expenses incurred by it in connection with the performance of this contract and such records shall be available for inspection of the Contracting Officer or his representative after the completion or earlier termination of this contract. Such cost data shall be for the information of the Government, but shall in no way affect the contract price of the articles, spare parts, supplies or work covered by this contract.

10. About April 1939, when the plaintiff received its contract for the production of service test models of the P-39 Airacobra, it began to fabricate and install permanent tooling for the production of this type of airplane. Production tooling is distinguished from ordinary machine tools, in that the latter are more permanent and universal in character, consisting of milling machines, lathes, drill presses, etc., not restricted in use to specific models or types of the product manufactured.

Production tooling for the P-39 pursuit fighter plane was largely assembly tooling, consisting of long-beam assembly, subassembly and tail-assembly fixtures, all of which were fabricated in structural steel and remained in use as long as this type of plane was in production. It also included metal tubes, angles, form blocks, jigs, router templets and templet dies. In the production of experimental models, most of these fixtures were fabricated in wood, and tooling was provided for temprorary use. But, in the production of service planes the plaintiff was required to provide for interchangeability of certain parts, such as wings, tails, and sur-
96 face landing gear, necessitating accurate duplications of the various parts.

As additional contracts for Airacobras were received during 1939 and 1940, the plaintiff increased its numbers of assemblies to provide for greater production and duplicated the tooling for such assemblies, subassemblies, and such auxiliary tooling as became necessary to meet increased production requirements. The plaintiff provided tooling for its Niagara Falls plant, which started operations in June 1941, similar to that it had installed in its Elmwood Avenue plant.

During 1939 and 1940, the plaintiff incurred costs for production tooling for the P-39 Airacobra in the sum of $1,894,109.57. In December 1940, the plaintiff recorded this sum in a deferred account, together with the deferred costs on experimental contracts, entitled "Experimental, Development and Production Tooling Expenses." The defendant's Army Audit Agency disallowed $19,383.80 of the deferred cost for tooling, leaving $1,874,725.77 for allocation to future production.

11. In addition to the special production tooling set forth in the preceding finding, a substantial amount of additional tooling was required in the fabrication of P-39 airplanes.

The plaintiff's estimated tool charges for the various fixed-price contracts, other than the deferred costs, totaled $2,597,435.40. Its actual tooling costs for fixed-price production, other than the deferred tooling, were $2,233,239.47.

Some of the tools which had been provided as a preliminary to production and deferred for allocations against future production, would become worn out by use or obsolete as a result of current changes in design. Some were reworked and others were scrapped and replaced. The costs of reworking or replacing original tooling would be charged against current production and would be included in the tool costs in the preceding paragraph.

12. In connection with plaintiff's quotations on each of the fixed-price contracts (Finding 9), except the last two British contracts, plaintiff submitted a breakdown of its estimated costs of production. At that time only a portion of the experimental and development costs had been determined and set up in the deferred
97 account. Likewise, the production tooling expense involved herein had not yet been determined or set up in the deferred account inasmuch as that expense grew largely out of the performance of the fixed-price contracts. Accordingly, the cost estimates submitted in connection with each of plaintiff's fixed-price contracts in 1939 and 1940 did not contain any provision for the amortization of any part of the deferred experimental development and production tooling costs.

AMORTIZATION OF EXPERIMENTAL, DEVELOPMENT AND PRODUCTION TOOLING EXPENSE

13. As of December 31, 1940, the plaintiff had capitalized and deferred experimental, development and production tooling expense, as follows:

	Amounts expended and deferred by plaintiff	Disallowed by Army Audit	Net amounts subject to amortization
Experimental and development expense (Finding 6)	$1,528,760.66	$29,021.43	$1,499,739.23
Production tooling for P-39's (Finding 10)	1,894,109.57	19,383.80	1,874,725.77
Total	$3,422,870.23	$48,405.23	$3,374,465.00

14. The plaintiff originally planned to amortize its deferred costs of $3,374,465 on the basis of the number of planes delivered and to be delivered on all production contracts on hand at the end

of each year, and by prorating such costs annually against deliveries made during the current year.

Under the aforesaid plan the amount of amortization applicable to each airplane produced and delivered would decrease from year to year in proportion to the total increase in the number of planes under contract at the end of each year. At the end of the year 1940, the plaintiff had contracted to deliver approximately 1600 airplanes under its fixed-price contracts.

15. During 1941, the plaintiff received an additional fixed-price contract W 535 ac-32 for 180 planes and equivalent in parts. This contract appears in the table of fixed-price contracts, Finding 9.

In the latter part of the same year, the plaintiff entered into
98 two cost-plus-fixed-fee contracts for 2,392 airplanes of a similar type. According to the plan of amortization above referred to, a portion of the deferred experimental, development, and production tooling costs would have been allocated to planes produced and delivered under these CPFF contracts. However, plaintiff's officials had been advised by Army Air Force officials that the deferred expenses in question might not be approved for reimbursement under the CPFF contracts being negotiated. In order to avoid any question of allowable reimbursements, plaintiff changed its original plan of amortization by limiting the allocation of the deferred charges to its fixed-price production contracts only. Accordingly, plaintiff added only the additional planes covered by the fixed-price contract entered into in 1941, and the amounts charged to each plane thereafter remained constant.

16. The plaintiff's annual reports which were prepared and certified to by Price, Waterhouse & Company, certified public accountants, contain the following explanatory comments regarding the treatment of experimental, development and production tooling costs:

ANNUAL REPORT FOR 1938

> The company, from its inception, has charged currently to costs of contracts in progress all experimental and development work as the contracts were completed. During the year 1938 substantial experimental and development work of basic future value to the company was accomplished in connection with a contract for the design and construction of an experimental airplane. The total expenditures, including the costs for basic development above referred to, charged to the costs of such contract, plus the estimated costs to complete, amounted to $128,052.77 over and above the contract price of the experimental plane. The sum of $128,052.77 was transferred to a deferred account at December 31, 1938.

ANNUAL REPORT FOR 1939

C—The deferred experimental and development expenses were in respect of two experimental airplanes.

The first of these (known as the Airacuda) was practically completed at December 31, 1937, and the estimated excess
99 of its cost over the contract sales price was charged to profit and loss accounts for the year 1937. Subsequent to the delivery of the airplane in 1938 expenditures were made in connection with improvements in design and in further development of this project. Such additional expenditures, amounting to $200,320.23 have been deferred at December 31, 1939, as, in the opinion of the management, the development of this type of airplane has a probable value to the Company in connection with expected future sales. A contract for 13 Airacudas for service test involving three experimental variations of the original Airacuda, now in progress, is expected to be completed during 1940. Since the date of closing the annual accounts the Company has made substantial expenditures, not theretofore anticipated, in connection with the contract for thirteen Airacudas. The amount of the total excess costs over the contract price has not been determined at this time.

The second of the experimental airplanes is being constructed for the Navy and the amount of $217,682.92 deferred in respect of this airplane is the excess of the estimated total cost when completed over the contract sales price. In the opinion of the management, such excess costs constitute development and experimental expenditures of value in connection with expected orders for this or similar types of aircraft.

The amount of $128,052.77 deferred at December 31, 1938, in respect of another experimental airplane has now been transferred to costs of airplanes of similar type for which contracts were received in 1939; accordingly the amount deferred at December 31, 1938, is included in the inventory of work in progress at December 31, 1939.

It is the Company's intention to charge the deferred experimental and development expenses to costs of future production (exclusive of the service test order above referred to) or, if and when the projects are abandoned, to charge them off to profit and loss accounts.

ANNUAL REPORT FOR 1940

During the past five years, the Company has developed three types of Airplanes known as Airacobra, Airacuda, and Airabonita, all three incorporating certain similar basic new developments. In the opinion of the management the excess costs

on experimental and service test contracts constitute experimental and development charges and, together with costs of tooling for production, have been deferred. Such costs amounted, in the aggregate, to $3,422,870.23 at December 31, 1940 and consisted of charges on the Airacobra of
100 $2,123,195.87, on the Airacuda of $889,499.48 and on the Airabonita of $410,174.88. The Company is at present concentrating on the manufacture of Airacobras, and it is the Company's intention to absorb the aggregate of the foregoing charges on the basis of the quantities of this model under contract. Amortization amounting to $70,773.45 has been charged against cost of goods sold in 1940.

ANNUAL REPORT FOR 1941

Experimental, development and production tooling expenditures amounting to $3,352,096.78 were deferred at December 31, 1940, to be absorbed on the basis of certain quantities of aircraft under contract. Of this amount an amortization of $1,998,184.02 applicable to aircraft delivered during 1941 was charged to cost of goods sold for that year.

During 1942, the plaintiff amortized the remaining experimental, development and production tooling costs in its deferred account against deliveries of airplanes under its fixed-price contracts.

17. Thus at the end of 1942, the plaintiff had amortized its entire deferred costs for experimental, development and production tooling against deliveries under its fixed-price contracts, as follows:

Contract number	1940	1941	1942	Totals
United States				
W 535 ac-12635	$27,880.45	$ 1,923.18	.....	$ 29,803.63
W 535 ac-13383	42,893.00	128,853.06	.....	171,746.06
W 535 ac-15675	.....	934,665.48	$382,712.82	1,317,378.30
W 535 ac-32	.....	.....	346,172.40	346,172.40
Totals	$70,773.45	$1,065,441.72	$ 728,885.22	$1,865,100.39
British				
A-218	.....	$ 369,250.56	$ 15,385.44	$ 384,636.00
A-1326	.....	405,790.98	75,004.02	480,795.00
A-1476	.....	157,700.76	534,638.08	692,338.94
Totals	.....	$ 932,742.30	$ 625,027.54	$1,557,769.94
Totals	$70,773.45	$1,998,184.02	$1,353,912.76	$3,422,870.23

COST-PLUS-FIXED-FEE CONTRACTS

18. In the meantime, commencing August 14, 1941, the plaintiff had entered into a series of cost-plus-fixed-fee, or CPFF, contracts with the defendant through the United States Army Air Corps for the production of P-39 or Airacobra airplanes.

101 Under the CPFF contracts the defendant agreed to reimburse the plaintiff for the cost of manufacturing and in addition to pay the plaintiff a fixed fee as provided in each of such contracts. The particular contracts, with dates of execution, are described in the following table:

Item	Date of contract	Contract numbers	Airplanes and equivalent in spare parts	Type	Estimated costs	Fixed fee specified
(I)...	8/14/41	W 535 ac-20910..	1,980	P-39D ...	$ 70,960,740	$ 4,257,644.40
(J)...	9/10/41	DA W 535 ac-156	412	P-39D-1 ..	14,985,926	899,155.56
(K)..	6/29/42	W 535 ac-29318..	2,700	P-39E	88,670,000	3,546,800.00
	4/13/45	Increase	2,470	P-63A-1 ..	64,814,800	2,592,592.00
(L)...	9/28/43	W 535 ac-40071..	2,600	P-39Q	68,387,200	2,735,488.00
Totals.....			10,162	.....	$307,818,666	$14,031,679.96

By supplemental agreement dated September 29, 1942, contract W 535 ac-29318 was changed to provide for deliveries of Model P-63A-1 in lieu of the P-39 type specified under the original contract. Contract W 535 ac-40041, dated January 5, 1944, for 2,470 planes and equivalent in spare parts, type P-63A-1, was combined on April 13, 1945, and made a part of contract W 535 ac-29318 and is represented by the increase as noted in the above table.

The production of P-39 models was discontinued in April 1944 on all of the above-described contracts and changed over to P-63 models on which production was thereafter continued.

Deliveries were completed under contract DA W 535 ac-156, W 535 ac-40071 was terminated November 3, 1944, and contracts W 535 ac-20910 and W 535 ac-29318 were terminated for the convenience of the Government August 14, 1945. Termination settlement agreements were consummated pursuant to the Contract Settlement Act of 1944.

19. Each of the CPFF contracts contains the following provisions:

ARTICLE 3. CONSIDERATION

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the Contract, subject to reimbursement for cost, as outlined in Article 6 hereof, the cost, plus a fixed fee of * * * being * * * percent of the total
102 estimated cost of * * *. This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of

the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

(b) For the purpose of determining the amount payable under this Contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

(1) All costs which have been incurred by the Contractor in anticipation of this Contract and prior to the signing thereof, and which if incurred after the signing of this Contract, would have been considered as allowable items of cost within the meaning of said Regulations, shall be considered as allowable items of cost incurred hereunder.

Article 3 (b) (2) of contracts W 535 ac–20910 and DA W 535 ac–156, and Article 3 (d) of contracts W 535 ac–29318 and W 535 ac–40071, provide:

(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this Article shall be included in determining the amount payable under this Contract, notwithstanding any provisions contained in the specifications or other documents incorporated in this Contract by reference, designating services to be performed or materials to be furnished by the Contractor at its epense or without cost to the Government.

Section 26.9 of Chapter 1 of Title 26, Code of Federal Regulations, as contained in T. D. 5000, is a promulgation of regulations governing the computation of Excess Profits Taxes, and provides, in part, as follows:

103 *Cost of performing a contract or subcontract*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract, and (2) the proper proportion of any

indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.

• • • • •

(e) *Factory cost.* • • •

(5) *Indirect factory expenses.*—Items, usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

• • • • •

(D) *Fixed charges and obsolescence.*—Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable standby equipment; and depreciation and obsolescence of special equipment and facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the Department concerned has made a certification binding upon the Commissioner of Internal Revenue, • • •

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current
104 charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is

carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

Said Section 26.9 of T. D. 5000 further provides in subparagraph (g) (4) thereof as follows:

• • • Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such cost, are the following: • • • losses on the other contracts; • • •

20. CPFF contracts W 535 ac-20910, DA W 535 ac-156, and W 535 ac-29318, provide in Articles 6, 16, and 17 (a) thereof as follows:

ARTICLE 6. PAYMENTS

(a) *Reimbursement for Cost.*—The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer, and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; • • •

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

105 ARTICLE 17. DEFINITIONS

(a) The term "head of the department" as used herein shall mean the head or any assistant head of the executive department or independent establishment involved, and the term "his duly authorized representative" shall mean any person authorized to act for him other than the Contracting Officer.

CPFF contract W 535 ac–40071 provides in Article 16 thereof, as follows:

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. * * * Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

REALLOCATION OF DEFERRED COSTS TO ALL PRODUCTION CONTRACTS

21. In 1942, at which time the plaintiff was engaged in production on CPFF contracts described in Finding 18, the Internal Revenue Bureau of the Treasury Department required that, for income tax purposes, the experimental, development and production tooling expenses should be allocated to airplanes produced under CPFF contracts as well as the fixed-price contracts.

106 A copy of a memorandum by Paul C. Gillette, Engineer Revenue Agent, dated March 12, 1942, in reference to the plaintiff's operations for the years 1939 and 1940, was furnished to the plaintiff. It contained the following recommendation:

That the entire costs at December 31, 1940, in the Development and Jig Expense Account, including the losses incurred, not charged off in prior years, on the Airacuda and Airabonita models, be amortized at a rate represented by the ratio of planes produced during the year compared with the total of planes produced and on order at the end of the year.

This recommendation was in harmony with the plaintiff's original plan of amortization.

The plaintiff declined to accept this recommendation and continued to amortize the remaining deferred charges for experimental,

development, and production tooling costs against the deliveries of airplanes under its fixed-price contracts during the remaining months of 1942, as set forth in Finding 17. The Bureau of Internal Revenue, however, adjusted the plaintiff's income for 1941 and 1942 for amortization by allocating such costs to deliveries under fixed-price contracts and deliveries made and to be made under CPFF contracts. Additional taxes assessed and paid for 1941 and 1942 totaled approximately $1,337,474.89.

22. On September 19, 1942, Charles L. Beard, then Secretary and Treasurer of the plaintiff corporation in a memorandum directed to John Berry, Jr., Comptroller of the plaintiff corporation, made *inter alia* the following statement of policy in connection with such deferred experimental, development and production tooling expenses as it related to the above-mentioned suggestion then being made by the Bureau of Internal Revenue:

> This item should be allowed as an amortization expense against the fixed price contracts only in view of the fact that any amortization to be allowable under a cost-plus-fixed-fee contract would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost plus contracts in view of the position taken by the Government that prior to our entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses.

107 On April 2, 1943, John Berry, Jr., prepared and submitted to the Resident Auditor, Army Air Forces, a "Statement of Accounting Policies, Pertinent to Operations Under Cost-Plus-A-Fixed-Fee Supply Contracts," in which he made the following statement in connection with deferred charges for experimental development and production tooling expense:

> 3. Deferred Charges.—
>
> • • • • •
>
> (c) Experimental, development and production tooling expenses are written off against the deliveries of the items to which expenditures apply. No experimental expense is charged to overhead applicable to CPFF contracts. • • •

23. On September 7, 1943, the plaintiff wrote to the Price Adjustment Board, War Department, New York City, an outline of its proposed future amortization of said deferred charges. Major Knox B. Phagan was at that time Army Air Corps Price Adjustment Officer. Said letter is as follows:

> Pursuant to our telephone conversation this afternoon, we should be glad if you would indicate your approval of the

method to be followed in amortizing development and experimental expenses and production tooling costs of P–39 airplanes.

Our records as of December 31, 1942, and the schedules originally submitted to you showed that we had amortized the full amount of these costs against fixed price contracts. You objected to such treatment on the ground that the costs should be amortized over cost plus a fixed fee as well as fixed price contracts. The Bureau of Internal Revenue in examining our Federal income and excess profits tax return for the calendar year 1941 had made the same objection and required us to amortize the costs over all airplane contracts then held by us. In view of the position taken by the Bureau of Internal Revenue and yourselves we have agreed to amortize the experimental and development expenditures over all contracts for P–39 and P–63 airplanes and the P–39 production tooling expenditures over all contracts for P–39 airplanes, provided that the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office.

108 Under date of August 14, 1943 we provided you with two schedules which set forth in detail the amounts and contracts involved in the write-off from January 1, 1940, to June 30, 1943, on an actual write-off basis and through the balance of 1943 and 1944 on an estimated basis.

The method agreed upon involved a determination of each of the two amounts involved, which amounts are as shown by our books (and less adjustments aggregating $2,892.19 are as shown by a report of an Agent of the Bureau of Internal Revenue as of December 31, 1940) less adjustments made by the Contract Audit Section of the Army Air Forces as a result of their examination of the costs. The amounts are as follows:

	Development and experimental	P–39 production tooling	Together
Costs to December 31, 1940 (There were no additions subsequently)	$1,528,760.66	$1,894,109.57	$3,422,870.23
Less—Costs disallowed by Contract Audit Section, Army Air Forces	29,021.43	19,383.80	48,405.23
Amount to be amortized as agreed upon with Price Adjustment Board and Contract Audit Section, Army Air Forces	1,499,739.23	1,874,725.77	3,374,465.00

The last amounts shown above are to be amortized over all fixed price and cost plus a fixed fee supply contracts for P–39 and P–63 airplanes as follows:

The sum of the number of airplanes and equivalents on order and undelivered at the beginning of the year and the number of airplanes and equivalents ordered during the calendar year is to be divided into the unamortized cost as of the beginning of the year, the resulting quotient represents the amortization per airplane. The amortization per airplane multiplied by the number of airplanes and equivalents accepted by the Army Air Forces during the period for each contract results in the amortization per contract.

We believe the foregoing sets forth the understanding between us as to the amortization of the expenditures for experimental and development and P–39 production tooling and if it is in accordance with your understanding we should like you to so indicate by signing one copy of this letter and returning it to us.

Yours very truly,

BELL AIRCRAFT CORPORATION,
(Signed) JOHN BERRY, JR.,
Comptroller.

109 The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

(Signed) KNOX B. PHAGAN,
Maj. A. C., Price Adj. Officer.

Date: Sept. 9, '43.

The plan of amortization outlined in the above letter is in accordance with the decision of the Internal Revenue Bureau. It was the plaintiff's original plan of amortizing these costs against production under fixed-price contracts before it had received any of its CPFF contracts. Major Phagan was then Chief of the Price Adjustment Section, Eastern District, Air Forces.

24. On September 9, 1943, the plaintiff's comptroller issued instructions for the restoration to the deferred account the proportion of experimental, development and production tooling which became applicable to airplanes delivered and to be delivered under the CPFF contracts, in accordance with the approved plan of reamortization. There was restored the sum of $2,286,819.95, consisting of:

Experimental and development costs	$1,035,918.73
Production tooling for P-39 planes	1,250,901.22

The unrestored difference of $1,087,645.05 previously amortized represented that portion of experimental, development and pro-

duction tooling which was applicable to deliveries under the fixed-price contracts in accordance with the approved plan of reamortization.

Reimbursement vouchers were prepared by the plaintiff and submitted in the sum of $451,179.96 for reallocation of amortization of experimental, development, and production tooling on deliveries under CPFF contracts during 1942 and $848,676.06 for deliveries under CPFF contracts during January to August, inclusive, of 1943, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$370,552.30	$819,571.64	$1,190,123.94
DA W 535 ac-156	37,318.96	72,413.12	109,732.08
Total	407,871.26	891,984.76	1,299,856.02

Defendant's Assistant Resident Auditor, Mr. DiLapo, considered the vouchers and recommended to the Resident Auditor, Mr.
110 Campbell, that they be rejected as not constituting costs allowable under the contract for the following reasons: that in the period prior to the inception of plaintiff's CPFF contracts, the contractor had followed a consistent policy of charging off all of these experimental, development, and production tooling expenses against its fixed-price contracts which were then in effect; that in the opinion of the assistant auditor there was no provision in the CPFF contracts for the re-imbursement to a contractor of *losses* suffered under fixed-price contracts and that these particular expenses were losses suffered by Bell in the performance of its fixed-price experimental contracts in 1936-1938. Mr. Campbell, the resident Auditor, did not agree with this position, and certified the vouchers to the Contracting Officer. The defendant's Contracting Officer approved the above vouchers for reimbursement under the CPFF contracts, and the plaintiff was paid the said sums by the defendant's Finance Officer.

25. Commencing in October 1943, the plaintiff submitted additional reimbursement vouchers for experimental, development, and tooling costs, representing the proportionate amounts applicable to deliveries subsequent to August 1943 under CPFF contrasts, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$194,947.81	$79,991.20	$274,939.01
DA W 535 ac-156	13,888.85	4,371.50	18,260.35
W 535 ac-29318	223,288.09	69,895.04	293,183.13
W 535 ac-40071	195,922.72	204,658.72	400,581.44
Total	628,047.47	358,916.46	986,963.93

The above sums represent vouchers for all of the remaining experimental, development, and production tooling costs for which the plaintiff claimed reimbursement. No part of these sums has been paid.

26. As these vouchers began to arrive for audit in October 1943 the defendant's Resident Auditor, Roland Campbell, had been replaced by Frank Ferris. About the same time, Bancroft Mitchell, the Contracting Officer for the plaintiff's CPFF contracts, was replaced by Maj. Harold B. Davies, who acted both as Ad-
111 ministrative Contracting Officer and Termination Contracting Officer.

The Assistant to the Resident Auditor, James D. DiLapo, again recommended against approval of these vouchers for reimbursement on the ground that the plaintiff had consistently charged its experimental, development and production tooling costs against deliveries under its fixed-price contracts, and for the further reason that DiLapo considered such costs as losses on other fixed-price experimental contracts which would not be reimbursable costs under CPFF contracts. Approval of these vouchers was withheld by Ferris.

In February 1944, the defendant's Resident Auditor Ferris was replaced by one Harry Leibman, who likewise withheld approval of these vouchers on the ground that the CPFF contracts contained no provision for payment of experimental, development and production tooling expenses, except by reference to T. D. 5000, and for the further reason that the plaintiff had previously amortized such costs against fixed-price contracts.

Major Davies declined to approve these vouchers, since these deferred costs had been previously amortized against deliveries under fixed-price contracts, and he thought the plaintiff had changed its method for the reamortization of such costs over all contracts as a result of the decision of the Bureau of Internal Revenue, but without the approval of the Contracting Officer.

27. In April and May 1944, the Chief Cost Auditor for the General Accounting Office, Buffalo area, submitted to the Resident Auditor a series of "informal inquiries" in respect to the reimbursements of experimental, development and production tooling costs by Col. J. Harris, Finance Officer, in August and September 1943, summarized in Finding 24, as follows:

		Reimbursement exceptions	
Informal inquiry	Dated	Contract	Total payments
777	4/25/44	W 535 ac-20910	$1,064,888.18
778	4/25/44	DA W 535 ac-156	109,732.08
789	5/13/44	W 535 ac-20910	125,235.76
Total (Finding 23)			1,299,856.02

112 Each of the foregoing inquiries made exception to such payments as follows:

Since the entire amount of the Deferred Experimental and Development Expenses and the Production Tool Expenses were amortized or written off against prior commercial and Government fixed price contracts by the contractor, the status of the account at the time of the negotiations with respect to the estimated costs under his contract was such as to preclude consideration thereof as an existing "Deferred" or "unliquidated" charge to the contract and the fact that for tax purposes the account was reopened and amortized in part against this contract would appear to afford no proper basis for considering the amount so amortized as a reimbursable item of cost under this contract.

28. By letters dated June 29, 1944, the Resident Auditor, Harry Leibman, advised the Chief Cost Auditor for the General Accounting Office at Buffalo that deductions were made on vouchers listed in the said letters to recover payments for experimental, development and production tooling costs, in accordance with informal inquiries 777, 778 and 789. Copies of these letters were furnished the plaintiff.

The Contracting Officer held up the vouchers on which the Resident Auditor made deductions, and took no action upon them until September 1944.

In the interim the Comptroller General of the United States issued formal notices of exception and suspensions of the accounts of Colonel J. Harris, Finance Officer at Buffalo, dated August 18, 1944. These notices covered the sums of $1,064,888.18 and $109,732.08, on which exceptions were noted by informal inquiries Nos. 777 and 778 and for the same reason. They were received by the Finance Officer August 21, 1944. Recoupment of these sums was made immediately by the Finance Officer on vouchers for monies otherwise due the plaintiff, and the Comptroller General was advised thereof by reply endorsements August 25, 1944.

On September 6 and 8, 1944, the Contracting Officer transmitted to the Finance Officer for settlement, groups of the plaintiff's vouchers, which included the vouchers on which deductions were made by the Resident Auditor, as above. The Contracting Officer reinstated vouchers for $1,064,888.18 and $109,732.08 for which sums had been recovered by the Finance Officer, but other
113 deductions for $125,235.76 were approved by him in compliance with informal inquiry and exception No. 789, and in harmony with the formal notices of exception and suspension previously received by the Finance Officer.

On September 12, 1944, the Finance Officer received a formal notice of suspension from the Comptroller General dated September 11th for the sum of $125,235.76, in accordance with informal inquiry No. 789. A reply endorsement was issued the following day by the Finance Officer for removal of the suspension since this sum had been deducted from vouchers for amounts otherwise due the plaintiff. Thus the payments totaling $1,299,856.02 for experimental, development and production tooling costs reimbursed to the plaintiff on CPFF contracts were fully recovered by the defendant.

29. Experimental, development, and production tooling costs which were amortized and vouchered for reimbursement by the plaintiff under CPFF contracts, Findings 24 and 25, are combined as follows:

Contract number	Experimental and development expense	Production tooling costs	Total
W 535 ac-20910	$565,500.11	$899,562.84	$1,465,062.95
DA W 535 ac-156	51,207.81	76,784.62	127,992.43
W 535 ac-29318	223,288.09	69,895.04	293,183.13
W 535 ac-40071	195,922.72	204,658.72	400,581.44
Total	1,035,918.73	1,250,901.22	2,286,819.95

30. The second Contracting Officer declined to approve the additional vouchers for $986,963.93 (Findings 25 and 26), and on January 10, 1945, he wrote to plaintiff stating that he was forwarding a copy of a decision by the Chief of the Procurement Division, which decision the Contracting Officer stated he was adopting as his findings of fact and decision in denying reimbursement to the contractor for the expenditure as requested on a covering list of Audit Bureau Vouchers. The enclosed decision of the Chief of the Procurement Division was dated November 13, 1944, and was apparently in response to a request for advice originating in a letter of December 10, 1943, from the Resident Auditor on the Bell project, forwarded under a subject heading reading
114 "Amortization of Losses on Fixed Price Contracts". The decision discussed generally the handling by Bell of the entire amount of experimental, development, and production tooling exepnses carried in the deferred account. It took the position that the profits earned by Bell on its *fixed price* production contracts were "more than enough to recover for Bell Aircraft Corporation the total amount of the expenditures of $3,422,870.23 • • • and were so treated on the books of Bell Aircraft Corporation"; that Bell had failed to show that it had not in fact recovered through the fixed-price production contracts the entire amount of such development expenses; that the $2,286,819.95 which Bell had

charged on its books against CPFF contracts did not, in fact, represent costs of performing such CPFF contracts, and that reimbursement for such costs under the CPFF contracts would result in Bell's receiving double payment from the Government. The letter concluded:

> It is therefore the opinion of this Headquarters that Bell is not entitled to reimbursement under its CPFF contracts for P–39 and P–63 airplanes for any portion of the said sum of $2,286.819.95.

On March 1, 1945, the second Contracting Officer wrote to plaintiff again stating that the findings of fact and decision which he had rendered on January 10, 1945, were rescinded and new findings and decision were forwarded. The new findings listed the same unpaid vouchers, and continued almost word for word in the same manner as the previous communication of January 10, except for the omission of the first paragraph which had related the circumstances under which the Chief of Procurement was rendering advice, and a change in the last paragraph of the "findings" so that it read , "It is, therefore, the decision of the Contracting Officer" rather than, "It is therefore the opinion of this Headquarters."

The sum of $2,286,819.95 mentioned in both sets of findings represents the $1,299,856.02 which had been approved by the predecessor Contracting Officer, paid, and recouped by the Finance Officer under suspension by the Comptroller General, as well as the unpaid vouchers totaling $986,963.93, summarized in Finding 25,
115 for which no payment had been made.

31. On March 27, 1945, the plaintiff made timely appeal from the findings and decision of the second Contracting Officer, in denying payment on vouchers totaling $986,963.93. The sum of $1,299,856.02, which had been previously reimbursed and was noted for exception and suspension of the accounts of the Finance Officer by the Comptroller General, was not appealed by the plaintiff nor considered by the War Department Board of Contract Appeals, representing the Secretary of War.

On April 29, 1946, the War Department Board of Contract Appeals rendered its decision on the plaintiff's appeal in which it denied the reimbursement of the said sum of $986,963.93. This decision states in part:

> All of the contracts contain a "Disputes" article and all of these articles except the one in Contract No. DA-W 535-ac-156 authorize the designation of a board as the representative of the Secretary of War to determine appeals from the decisions of the contracting officer. The mentioned contract provides

only for appeal to the head of the department or his duly authorized representative. Insofar as the questions presented by this appeal are questions of law they will be administratively determined pursuant to the memorandum of Secretary of War dated 4 July 1944.

There is no dispute between the parties as to the amount of the costs or as to the propriety of the method of allocation used by appellant. The only question presented is whether reimbursement for any portion of these costs is authorized or required by the subject contracts under the circumstances here involved. The subject contracts do not expressly provide for reimbursement of these costs but provide that allowable items of cost will be determined by the contracting officer in accordance with the provisions of T. D. 5000.

The experimental and development costs are clearly within the category of indirect costs as defined by T. D. 5000 and are specifically covered by Section 26.9 (d) of T. D. 5000—set out above. There is no specific reference in T. D. 5000 to the amortization of production tooling costs and appellant has not pointed out a specific provision of T. D. 5000 which it considers as providing for the allowance of such an item of cost. In the pamphlet issued by the War and Navy Departments
116 entitled "Explanation of Principles for Determination of Costs Under Government Contracts" (Par. 18), it is indicated that items such as royalties and the amortization of the initial cost of dies, patterns, and special tools can logically be classified as direct shop costs and be charged to contracts on an equitable basis of apportionment. Section 26.9 (e) (5) (D) of T. D. 5000 set out above also provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. It is clear from the record and evidence that the production tooling was used in the performance of CPFF contracts calling for the production of the P-39 type of airplane. It would seem, therefore, that items of this type are within the intent and meaning of T. D. 5000.

• • • • •

Although it is true that costs of this type may properly be allowed as reimbursable items under T. D. 5000, it does not follow that such costs must be reimbursed under T. D. 5000 in all cases and under all circumstances. In order to determine whether such items of costs should be reimbursed it is necessary to examine all of the circumstances and facts involved. The subject costs—both engineering and development, and

production tooling costs—were incurred a considerable time before any of the CPFF contracts were entered into. The production tooling costs were incurred for the express and admitted purpose of performing certain fixed-price contracts then on hand or in process of negotiation. They were not incurred in anticipation of the CPFF contracts and would have necessarily been incurred regardless of whether any further contracts for the P-39 type of airplane were received or not. The engineering and development costs were incurred during the period 1938 to 1940 and the costs were capitalized because it was felt that the development in connection with which they were incurred had a probable value in connection with expected future sales. In 1940 appellant entered upon a course of conduct by which these costs were charged against certain fixed-price contracts. The procedure of charging these costs against fixed-price contracts was continued during 1941 and 1942 in accordance with the mentioned plan to the effect that at the end of 1942 all of the costs in question had been absorbed. During this period some of the subject CPFF contracts were entered into and all of them were negotiated prior to August of 1943 at which time appellant changed its plan of amortization to the one now contended for. It is clear from the record that no portion of these costs was in-
117 cluded in the estimates under the CPFF contracts and no specific consideration was given to the question of reimbursement in the negotiation of the subject contracts. It also may be reasonably concluded that appellant had no intention, at the time the contracts were entered into, of seeking reimbursement for such costs since its accounting method did not contemplate reimbursement.

* * * * *

Under these circumstances, it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated, appellant did not intend that the item should be reimbursable and was in fact charging the costs in question against other contracts in accordance with a previously adopted plan. The contracting officer in effect has found that the costs in question were in fact recovered by appellant through the fixed-price contracts. Although appellant states that these costs were not specifically set out as such in the quotations on the fixed-price contracts, it produced no evidence that these costs were not in fact recovered under the fixed-price contracts. Under the circum-

stances here present, the Board is of the opinion that the costs are not reimbursable under the subject contracts.

* * * * *

For the reasons herein set out the appeal insofar as it relates to contracts numbered W 535-ac-20910, W 535-ac-29318, W 535-ac-40071, and W 535-ac-40041 is denied.

In respect to contract DA W 535 ac-156, the President of the Board, the duly authorized representative of the Secretary of War, decided in accordance with the entire Board on other contracts, and denied the plaintiff's appeal insofar as it related to this contract.

The plaintiff's application for a rehearing was denied by the Board May 31, 1946.

32. Upon the termination of hostilities, plaintiff's CPFF contracts then in progress were terminated for the convenience of the Government. Termination settlement agreements were entered into pursuant to the Contract Settlement Act of 1944, in which plaintiff made reservations in respect to its claims for reimbursements under the CPFF contracts, as follows:

118 The Supplemental Settlement Agreement dated December 21, 1945, covering the termination of contract W 535 ac-20910, contains the following reservation in Article 4 (c) (2) (b):

> Claim for experimental and development and research costs in the amount of $1,465,062.95 which is now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated May 15, 1946, covering the termination of contract W 535 ac-29318, contains the following reservation in Article 4 (c) (2) (b):

> $293,183.13 of experimental and development expenses now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated February 22, 1946, covering the termination of contract W 535 ac-40071, contains the following reservation in Article 4 (c) (2):

> Claim by the Contractor against the Government, as to which his right of reimbursement is disputed, which is excluded without prejudice to the rights of either party, to wit, claim for experimental and development and research costs in the amount of $400,581.44, which is now the subject of an

appeal pending before the War Department Board of Contract Appeals.

At the time the settlement agreement was consummated for contract W 535 ac-20910, there was pending before the War Department Board of Contract Appeals the plaintiff's claim for reimbursement of costs for $274,939.01. The difference of $1,190,123.94 had been reimbursed to the plaintiff, but was recouped by the Finance Officer upon notice of exceptions and suspension by the Comptroller General.

33. On March 27, 1945, the plaintiff executed a renegotiation agreement pursuant to Section 403 of the Sixth Supplemental National Defense Appropriation Act, 1942, as amended, in respect to excessive profits for its fiscal year ending December 31, 1942. This agreement was signed by Colonel Maurice Hirsch, G. S. C., for all services of the United States concerned, and was approved for the Under Secretary of War May 22, 1945.

119 The said agreement covered profits for 1942 on both fixed-price contracts and CPFF contracts with the United States. It provided for refund by the plaintiff of $7,714,000 of excessive profits for the year 1942, after first applying the tax credit applicable to such profits. This agreement provides in part: (See also Finding 17 herein.)

EXHIBIT "C"

* * * * *

PRINCIPLES UNDERLYING SEGREGATION OF SALES AND PROFITS

* * * * *

Allocation of Cost of Sales and Expenses

1. *Cost of sales*:

* * * * *

(g) Deferred Experimental Development, and Production Tooling Expenses in the amount of $1,353,913 were amortized over all planes delivered under Fixed Price Contracts during the year. For the purpose of computing the additional refund under Paragraph VIII of the Agreement, the adjusted amortization chargeable to 1942 of $638,683 was allocated on the basis of the total number of planes delivered under all contracts, both Fixed Price and CPFF.

* * * * *

VIII. In arriving at the refund herein the items of Deferred Experimental Development, and Production Tooling Expenses

in the amount of $728,885.22 have been charged as Costs against Renegotiable Fixed Price Contracts for said fiscal year. The Contractor, in order to conform its method of handling these items to the method adopted by the Bureau of Internal Revenue, has adjusted its figures for said fiscal year by amortizing these items over the total number of planes of the Airacobra type produced, or to be produced, on both Fixed Price and CPFF Contracts (Production Tooling limited to P-39 Models). Such method of amortization and the corresponding reallocation of costs to CPFF Contracts, as well as Fixed Price Contracts, has been tentatively approved by the Army Air Forces, and if the amount allocated to the CPFF Contracts is finally approved by both the Army Air Forces and the General Accounting Office of the Comptroller General of the United States, and reimbursement therefor, is made, the Contractor agrees to pay to the United States as an additional refund the sum of $667,000, on account of which the Contractor shall
120 receive credit for Federal Income and Excess Profits Taxes thereon as determined by the Bureau of Internal Revenue as provided in Paragraph VII hereof.

34. The amortization allowance of experimental, development and the production tooling to fixed-price contracts only, under the foregoing settlement agreement was contrary to the allocations by the Bureau of Internal Revenue, which amortized these costs upon production for all contracts.

By reallocating $2,286,819.95 of the $3,374,465.00 of deferred expense to the CPFF contracts, plaintiff's income from its fixed-price contracts was increased by such amount and the Bureau of Internal Revenue made additional assessments against plaintiff's resulting net income for 1941 and 1942 in the approximate sum of $1,337,474.89. The amount of $2,286,819.95 which the Bureau had disallowed as a cost deduction from the fixed-price contract income in 1941 and 1942, was allowed as a deduction from plaintiff's net income for the years 1943, 1944, and 1945 as costs of performing its CPFF contracts, making plaintiff's taxes for those years approximately $1,305,418.72 less than they would have been had such cost deductions not been allowed or had the $2,286,819.95 been reimbursed by the Air Forces as allowable costs under the CPFF contracts.

It is plaintiff's position that the $2,286,819.95 allowed by the Bureau as a cost deduction from CPFF income for 1943, 1944, and 1945, was in fact a reimbursable item of cost under those contracts. Had plaintiff received reimbursements of the $2,286,819.95 under its CPFF contracts, its net income for tax purposes for the years

1943, 1944, and 1945, would have been greater by that amount and it would have had to pay an additional $1,305,418.72 in taxes, but it would have saved $981,401.23, the difference between the $2,286,819.95 reimbursed, and the $1,305,418.72 which plaintiff would have paid in additional taxes.

VALUE OF EXPERIMENTAL AND DEVELOPMENT WORK TO COST-PLUS-FIXED-FEE CONTRACTS

35. Experimental and development costs capitalized and deferred by the plaintiff for allocation to future production were not segregated as between specific experimental contracts to which
121 they might apply. It was impossible to make any reasonably correct segregation of such costs, since the improvements in design and fabrication developed in the earlier operations were carried forward and applied on later experimental and development work, and finally into production contracts. These costs represent deferred values of designing and experience in fabrication rather than costs of any particular airplane contract.

The plaintiff took over the plant on Elmwood Avenue, Buffalo, New York, in the fall of 1935, which had been vacated by Consolidated Aircraft Company upon its transfer to California, and an abundance of experienced personnel who elected to remain in Buffalo.

The plaintiff's first work involved the installation of an Allison model engine in the nose of a Consolidated airplane. It was the first installation of this kind for the Allison model, which was a heavy 1,000 h. p. engine, whereas other models previously used were normally about 600 h. p. models. It required investigation of the strength of the wings, tail, fuselage and landing gear. The plaintiff's next job was subcontract work for manufacturing all-metal, aluminum, riveted wings for Consolidated flying boats.

The first experimental plane was the XFM-1 Airacuda contracted for May 12, 1936. It was substantially completed by the end of 1937. All costs of experimental and development work on the above projects were charged against these contracts currently or to the plaintiff's profit and loss account, up to and including December 31, 1937. The plaintiff continued further development work on the XFM-1 model in 1938, and later on a contract for service test models of the same type.

36. Some of the basic principles of design and fabrication, which the plaintiff developed on experimental contract work and incorporated into the P-39 production models, include the following:

(a) The installation and successful operation of a liquid-cooled Allison engine, involving installation problems and other features of design necessary to operations.

(b) The extension of the drive shaft, so that the propellers could operate more distant from the engine.

122 This feature was designed on the XFM-1, where the engine was housed in the wing structure, and the pusher-type propellers operated from the rear of the wings. The extension drive shaft was adopted in the P-39, by locating the engine in the fuselage to the rear of the pilot, with the extended drive shaft projected beneath the pilot and operating the propeller in the nose of the aircraft, thereby providing vision for the pilot and permitting the projecting nose of the plane to better accommodate the front wheel of the tricycle landing gear.

(c) The design and successfal installation of air intake ducts for cooling the engine and oil systems, known as "ducted radiator", whereby an intake opening was provided in the leading edge of the wing for admitting air at high velocity.

The air then expanded into larger internal ducts slowing down its velocity for cooling purposes. The overhead air scoop was subsequently incorporated in all P-39's and P-63 planes. The intake was provided on top of these planes, instead of the front edge of the wing, but serving the same purpose of obtaining a simple duct system of air intake to the carburetor of the engine.

(d) The development and installation of a successful anti-shimmy dampening device for the nose wheel of the tricycle landing gear.

The nose wheel of this type of gear was provided with a swivel stirrup to steer the plane on the ground. The nose-wheel shimmy or oscillation was inherent in this type of gear, as the plane would take the runway at high speed or over rough roads. The first successful development of the shimmy dampening device was in connection with the XP-39, although the basic characteristics in this device were developed by the plaintiff in connection with the development and installation of a shock-absorbing gun mount for the XFM-1 plane.

(e) The successful installation of a 37mm. repeating cannon in the XFM-1.

In the flexible gun mountings for the Airacudas the plaintiff devised means of holding and supporting the gun so that it could be properly aimed and provided for the recoil in this type

123 mounting. In the P-39's it was installed in a fixed mounting, but other features of feeding and ejecting the heavy empty cartridges were retained. Provision was made for retaining in the plane the empty shells that were ejected from the cannon, to avoid fouling or damage to the plane when they were

ejected. In lieu of clips, which required manual changing, the plaintiff devised an automatic feed belt to carry the shells into firing position.

(f) Flush riveting, which was developed in the earliest experimental planes, was carried into all later production.

A high-strength aluminum alloy was specified for the XFM-1 fighter plane built by the plaintiff under its first experimental contract. In order to take advantage of the higher structural tensility of this material the plaintiff, by a process of heat treating, sunk the rivets approximately flush with the surface of the metal, which resulted in a smoother external surface in this type of fabrication.

(g) In the construction of the XFL-1 Airabonita, the plaintiff designed and provided very heavy-duty landing gear to accommodate, without undue hazard, the catapult, deck landing and arresting equipment. This tougher type of landing gear was subsequently provided for P-39 models using the tricycle landing gear.

In connection with the XFL-1 for the Navy, the plaintiff also developed a nose-over beam, which extended in the fuselage above and behind the pilot for his protection in case the plane turned over. This feature was also incorporated in the production models of P-39 Airocobras.

(h) Engineering standards which were prepared for experimental work, consisting of short-cut repeat operations, tables and curves of technical information.

Once computed, these standards could be applied thereafter without recalculations.

(i) The earlier Allison engines furnished the plaintiff attained their greatest power at sea level.

In order to give them more power at high altitudes, the plaintiff installed General Electric turbo superchargers which were operated from the engines. Later Allison engines incorporated features to provide power at high altitudes, which duplicated the external unit and voided its further use.

124 (j) The plaintiff also developed and provided compartments in the wing structure of the experimental planes for carrying additional fuel, known as integral fuel tanks.

They were designed to be liquid tight and were enclosed by integral parts of the plane structure, such as the inside beams, bulkhead and outside sheeting. This feature was installed in P-39 models but it was not satisfactorily perfected because of difficulty

with leakage, and was later superseded with bullet-proof storage tanks, by fitting the compartments with rubber and composition cells that would self seal any bullet penetration.

With the exception of the last two features above, the developments, engineering standards and fabricating processes acquired during the manufacture of experimental airplanes were incorporated and utilized on all production. The measure of value to production after 1940 is represented by the plaintiff's excess of costs on experimental airplanes over and above its recoveries under these contracts in the net amount of $1,499,739.23.

37. The plaintiff obtained a basic patent on its development of a hydraulic shimmy-dampening device in the steering mechanism of the nose wheel of the tricycle landing gear, and certain other patents for semi-automatic counter sinkers, twisted spar mills, routers and stake drills. It recovered substantial royalty payments for use of these devices by another manufacturer. As a result of proceedings before a Royalty Adjustment Board, the plaintiff was required to pay over to the Government some $691,666.24, under an indemnity agreement with the War and Navy Departments, representing all royalties collected by it.

There was included in the sums paid over one amount of $102,050.28, which the plaintiff had previously taken into its income and paid taxes thereon. The tax rate during the war years averaged approximately 70 percent of the plaintiff's total net income. No part of the royalties collected was retained by the plaintiff.

The Government also received credit of $360,000 on a contract for an improved model of the P-39, pursuant to an agreement with the plaintiff dated April 11, 1940, which authorized the plaintiff to make certain deliveries to the British of the P-39
125 model airplanes in advance of deliveries under one of the production contracts for the Army Air Corps.

38. After having amortized the total amount of experimental development and production tooling expenses against its fixed-price production contracts, the plaintiff realized a net profit, before taxes and renegotiation of excess profits, of $18,280,732.50.

39. The plaintiff's net income on its fixed-price production contracts, after renegotiation and taxes, was approximately $4,637,607.63.

40. The sum of $1,499,739.23, which was capitalized and deferred by the plaintiff for allocation to future production, represented a fair and reasonable value of the general experimental

and development work in benefits and savings on production contracts.

VALUE OF PRODUCTION TOOLING TO COST-PLUS-FIXED-FEE CONTRACTS

41. Production tooling for the P-39 model was provided during 1939 and 1940. At the end of 1940, the plaintiff capitalized and deferred for allocation to future operations, production tooling costs totaling $1,874,725.77.

This production tooling was used for the fabrication and assembly of airplanes under all of the fixed-price production contracts. Some of the tools other than assembly fixtures became worn out through use or became obsolete on account of current changes from time to time during production.

The major portion of tooling for the P-39 models was used throughout the production of this type of plane under the CPFF contracts. Where replacements or reworking of tools became necessary, the costs were charged against current operations, so that when production under CPFF contracts was commenced the value of prodution tooling was substantially the same as when it was originally installed for use on fixed-price contracts.

In April 1944, the P-39 model was discontinued, and retooling became necessary for the production of P-63 models. All tooling which could not be used in the production of the later model was scrapped and replaced upon approval of the defendant's plant clearance officer.

126 Lists of tools and equipment which could no longer be used on the new models were prepared by the plaintiff, and allocated to certain of the CPFF contracts then in process. The proceeds of the sale of these tools and fixtures were credited to the defendant on CPFF contracts.

The beneficial value of production tooling for P-39 model airplanes manufactured under CPFF contracts was at least equivalent to the beneficial use of such tooling to performance under the fixed-price production contracts.

42. In submitting bids for its fixed-price contracts the plaintiff also submitted data of estimated costs of performing these contracts, the details of which are appended to copies of these contracts. None of the estimates for performing the fixed-price contracts contain any provision for the amortization of experimental, development and production tooling costs.

Estimated costs in the cost-plus-fixed-fee contracts, as specified in Article 2 thereof, were based upon data on file in the office of the Chief of Air Corps, no details of which were attached to these contracts. There is no evidence that these data contained any

estimate for the experimental, development and production tooling costs involved herein.

Article 3 (a) of the CPFF contracts provided for a fixed fee to the plaintiff of 6 percent of the estimated costs under the first two of these contracts and 4 percent of the estimated costs under the last two thereof. This Article contains the additional provision:

> • • • This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof; provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

The provisions for allowable costs are contained in the same article.

The plaintiff reamortized its deferred costs for experimental, development and production tooling expense over all production contracts, as follows:

127

	Fixed-price contracts (Findings 13 and 24)	CPFF contracts (Finding 29)
Experimental and development expense	$463,820.50	$1,035,918.73
Production tooling expense	623,824.55	1,250,901.22
	1,087,645.05	2,286,819.95

The amortization of $1,087,645.05 represents 1.52 percent of the total $71,364,004.86 value of fixed-price contracts, all of which were completed. The amortization of $2,286,819.95 on CPFF contract production represents .71 percent of the total estimated cost plus the fixed fees specified in these contracts. Deliveries called for under CPFF contracts were not completed and the contracts were terminated upon cessation of hostilities August 14, 1945.

Plaintiff's experimental, development, and production tooling costs were properly deferred as intangible capital assets and were properly chargeable as costs of any future production of products for the purpose of which such costs were originally incurred. The amortization of these intangible assets was ratably applied to the total number of P-39 airplanes produced, in accordance with a reasonably consistent plan.

CONCLUSION OF LAW

Upon the foregoing special findings of fact which are made a part of the judgment herein, the Court concludes as a matter of law that plaintiff is entitled to recover $2,286,819.95. It is therefore adjudged and ordered that plaintiff recover of and from the United States the sum of two million two hundred eighty-six thousand eight hundred nineteen dollars and ninety-five cents ($2,286,819.95).

OPINION

HOWELL, *Judge*, delivered the opinion of the court:

Plaintiff sues to recover $2,286,819.95 alleged to be reimbursable items of cost incurred in the performance of four cost-plus-a-fixed-fee contracts (hereinafter referred to as CPFF contracts) for the manufacture and delivery of military aircraft known as P-39's or Airacobras, entered into with defendant through the United States Army Air Corps.[1]

128 Of the total sum claimed to be due under the contracts, $1,035,918.73 represent experimental and development expense, and $1,250,901.22 represent production tooling cost.[2] It is plaintiff's contention that the sum in suit represents allowable costs which should have been reimbursed pursuant to all four CPFF contracts which provide in pertinent part as follows:

> ARTICLE 3 (b). For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. * * *
>
> ARTICLE 6—*Payments.*
>
> (a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; * * *

[1] Pertinent details concerning these four contracts are set forth in Finding No. 18.

[2] Finding No. 29.

Pertinent portions of T. D. 5000, referred to in Article 3 (b) are as follows:

SEC. 26.9. *Cost of performing a contract or subcontract*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract, and (2) the proper proportion of any indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.

* * * * *

(c) *Factory cost.*

* * * * *

(5) *Indirect factory expenses.*—Items usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but
129 which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

* * * * *

(D) *Fixed charges and obsolescence.*—Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable standby equipment; and depreciation and obsolescence of special equipment and facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the Department concerned has made a certification binding upon the Commissioner of Internal Revenue, pursuant to section 4 of the Act, in the case of such contract or subcontract. * * *

* * * * *

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties

and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expense which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expense or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project
130 may be allowed as a part of the cost of performing the contract.

Most of the experimental and development costs herein were incurred by plaintiff in the performance of certain fixed-price experimental contracts entered into with defendant in 1936, 1937, and 1938, for the construction of experimental and service test airplanes known as the "Airacuda", the "Airacobra" and the "Airabonita". (Findings Nos. 3, 4 and 5.) Subsequent to deliveries under these contracts, plaintiff incurred additional expense for further development and improvement of the design of the Airacuda (Finding No. 6). In the case of each experimental contract, the contract price agreed to and paid by defendant represented only a portion of the cost to plaintiff of performance. These excess costs and the later costs of further developing and improving the designs, were capitalized by plaintiff as deferred charges in 1938, 1939, and 1940 for later distribution as an element of cost against future production of the type of plane to which the experiments related.

Plaintiff's auditors allocated the deferred experimental and development costs to the three types of planes, and after deducting a sum disallowed by defendant's Army Audit Agency, there remained in the deferred account $1,499,739.23 (Finding No. 6). Plaintiff received no production contracts for Airacudas or Airabonitas, but it did receive many contracts for the Airacobra or P-39 pursuit fighter plane.

Plaintiff's production tooling costs involved in this suit were incurred first in April 1939, in connection with the performance of its contract with defendant for the production of thirteen service test models of the Airacobra (P-39). Production tooling is restricted in use to specific models or types of the product manufactured and is not as permanent and universal in character as are ordinary machine tools. Production tooling for the Airacobra or P-39 pursuit fighter plane was largely assembly tooling, consisting of long-beam assembly, subassembly and tail-assembly fixtures, all of which were fabricated in structural steel and remained in use as long as this type of plane was in production. It also included metal tubes, angles, form blocks, jigs, router templets and templet dies. In the earlier production of the experi-
131 mental models, most of these fixtures had been fabricated in wood and the tooling was for temporary use only. In the production of the service planes, plaintiff was required to provide for interchangeability of certain parts, such as wings, tails, and surface landing gear, necessitating accurate duplications of the various parts. Subsequent to the April 1939 contract, plaintiff received from the defendant additional fixed-price production contracts for Airacobras during 1939 and 1940 (Finding No. 9) and accordingly plaintiff increased its number of assemblies to provide for greater production, and duplicated the tooling for such assemblies, subassemblies, and such auxiliary tooling as became necessary to meet the increased production requirements.

During 1939 and 1940, plaintiff incurred costs for production tooling for the P-39 Airacobra in the sum of $1,894,109.57 and in December 1940, plaintiff recorded this sum in the deferred account along with the deferred costs of the experimental and development work. This account was entitled "Experimental, Development, and Production Tooling Expenses." Defendant's Army Audit Agency disallowed $19,383.80 of the deferred tooling costs so recorded, leaving in the account $1,874,725.77 for allocation to future production (Finding No. 10).

In connection with the several fixed-price production contracts for P-39's entered into by plaintiff and defendant in 1939 and 1940, plaintiff was required to submit breakdowns of its estimated costs of production. At the time of the contract negotiations, only a portion of plaintiff's experimental and development costs had been determined and set up in the deferred account. Likewise, the production tooling expense involved herein had not yet been determined and set up in the deferred account inasmuch as that expense grew largely out of plaintiff's performance of those fixed-price contracts. Accordingly, the cost estimates submitted in connection with each of plaintiff's fixed-fee contracts in 1939 and 1940 did

not contain any provision for the amortization of any part of the deferred experimental, development, and production tooling costs.

132 As of December 31, 1940, plaintiff had capitalized and deferred its experimental, development, and production tooling expense as follows (Finding No. 13):

Experimental and development expense	*$1,499,729.23
Production tooling for P-39's	*1,874,725.77
Total	*3,374,465.00

* (These are the amounts approved by the Army Audit Agency, referred to above.)

Plaintiff first planned to amortize its deferred experimental, development, and production tooling expenses on the basis of the total number of planes delivered and to be delivered on all contracts on hand at the end of each year, and by prorating such costs annually against deliveries made during the current year (Finding No. 14). Under this plan, the amount of amortization applicable to each airplane produced and delivered would decrease from year to year in proportion to the total increase in the number of planes under contract at the end of each year. At the end of 1940, plaintiff had contracted to deliver approximately 1,600 airplanes under fixed-price contracts, and in 1941 plaintiff received an additional fixed-price contract for 180 planes and parts. In the latter part of 1941 plaintiff and defendant entered into the first two CPFF contracts for 2,392 airplanes of a type similar to those produced and delivered under the aforementioned fixed-price contracts.

Plaintiff's officials were not certain that the deferred experimental, development and production tooling expense would be approved for reimbursement under their CPFF contracts as allowable costs. Accordingly, in order to avoid any question of the reimbursability of such items, plaintiff abandoned its original plan of amortization of these expenses over *all* related production and decided to amortize such deferred expense to the airplanes produced and delivered under the fixed-price contracts only (including the fixed-price contract entered into in 1941) (Findings Nos. 15 and 16). By the end of 1942, plaintiff had amortized the entire amount carried in its deferred account against deliveries of airplanes under its fixed-price contracts (Finding No. 17).

Commencing on August 14, 1941, plaintiff entered into a series of cost-plus-a-fixed-fee contracts with defendants for the
133 production of P-39 (Airacobra) airplanes.[3] One contract was ultimately completed, one was terminated, and two were

[3] Data concerning the dates, quantities, estimated costs and specified fixed fees, are contained in a table in Finding No. 18.

terminated for the convenience of the Government on August 14, 1945, with termination settlement agreements consummated pursuant to the Contract Settlement Act of 1944 (Finding No. 18).

As stated above, by the end of 1942 plaintiff had allocated all of its deferred experimental and production tooling expenses to production under its fixed-price contracts although the items being produced under the CPFF contracts bore as close a relation to such deferred expenses as did the items produced under the fixed-price contracts. In 1942 the Bureau of Internal Revenue of the Treasury Department insisted that for income tax purposes, the deferred expenses in question should have been allocated to planes produced under the CPFF contracts as well as to planes produced under the fixed-price contracts, and, despite plaintiff's protests, the Bureau adjusted plaintiff's income for 1941 and 1942 for amortization purposes by reallocating such expenses to deliveries made under both types of contracts, and allowing as a cost deduction, only a portion of the deferred expense. This reallocation increased the amount of plaintiff's taxable income for these years, and additional taxes were assessed and paid for those years in the approximate amount of $1,337,474.89 (Finding No. 34).

In 1943, Major Knox B. Phagan organized defendant's contract renegotiation activities in the Eastern District Air Forces. Such activities were handled by the Price Adjustment Section of which Major Phagan was Chief. In 1943, the renegotiation of plaintiff's profits on its fixed-price contracts came before that Section. It was the purpose of that Section to make a fair determination of a war contractor's profits in order to determine whether or not such profits were excessive and should be paid back to the Government under the Renegotiation Act of 1942 (56 Stat. 245, 50 USCA § 1191). Major Phagan testified that his attention had been called to the action of the Bureau of Internal Revenue in disallowing the allocation by plaintiff of *all* of its deferred experimental,
134 development, and production tooling expenses to production under its fixed-price contracts, and stated that in general it was the policy of the Price Adjustment Section to follow the decisions of the Bureau of Internal Revenue in such matters for the purposes of renegotiation. Accordingly, the Price Adjustment Section took the position that plaintiff's allocation of all its deferred experimental, development, and production tooling expense to its fixed-price production alone, improperly reduced plaintiff's actual profits on such fixed-price contracts, and that such expenses should have been amortized over production under the cost-plus as well as the fixed-price contracts. Compliance with the position of the Price Adjustment Section, would have resulted in defendant's recouping much larger sums as excessive profits on plaintiff's 1942 income.

On September 7, 1943, plaintiff, by its Comptroller, wrote to the Price Adjustment Board, War Department, setting forth the facts concerning its treatment of the expenses in the deferred account, and stating that Bell was prepared to change its method of amortizing such deferred expense to conform to the views expressed by the Bureau of Internal Revenue and the Price Adjustment Board on condition that the proportion of the deferred expense disallowed by the Board and the Bureau on the ground that it was properly allocable to CPFF production, should become items of reimbursable costs under Bell's CPFF contracts and be allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office (Finding No. 23). On receipt of plaintiff's letter, Major Phagan caused the following statement to be placed on a copy of the letter which he then signed and returned to plaintiff:

> The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

On September 9, 1943, in accordance with the views of the Bureau of Internal Revenue and the Price Adjustment Board, plaintiff restored to its deferred account the proportion of experimental, development, and production tooling expense which it had been agreed were applicable to airplanes delivered and to be de-
135 livered under plaintiff's CPFF contracts, as follows:

Experimental and development costs	$1,035,918.73
Production tooling for P-39 planes	1,250,901.22

The unrestored difference of $1,087,645.05 previously amortized, represented that portion of experimental, development and production tooling expense which was properly applicable to deliveries under plaintiff's fixed-price contracts in accordance with the approved plan of reamortization.

Plaintiff then prepared and submitted for the approval of the Contracting Officer, reimbursement vouchers in the sum of $451,179.96 representing the reallocation of its amortization of experimental, development, and production tooling deferred expense to deliveries under its CPFF contracts during 1942, and vouchers in the sum of $848,676.06 applicable to deliveries under it CPFF contracts during the period from January to August, inclusive, of 1943 (Finding No. 24). Defendant's Assistant Resident Auditor, Mr. DiLapo, considered the vouchers and recommended to the Resident Auditor, Mr. Campbell, that they be rejected as not constituting costs allowable under the contract for the following reasons: that in the period prior to the inception of the CPFF contracts, the contractor had followed a consistent policy of charging off all of these experimental, development, and production tooling ex-

penses against its fixed-price contracts which were then in effect; that in the opinion of the assistant auditor there was no provision in the CPFF contracts for the reimbursement to a contractor of *losses* suffered under fixed-price contracts (referring to Bell's prior fixed-price experimental contracts in 1936-1938). It would appear that Mr. DiLapo had in mind Section 26.9 (g) (4) of T. D. 5000 which provided in part as follows:

> Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such costs, are the following: * * * losses on the other contracts: * * *

Mr. Campbell, the Resident Auditor, did not agree with this position and certified the vouchers to the Contracting Officer, Mr. Bancroft Mitchell. The Contracting Officer approved the vouchers for reimbursement under the CPFF contracts and plaintiff was
136 paid the sums shown thereon, totalling $1,299,856.02, by defendant's Finance Officer.

Commencing in October 1943, plaintiff submitted additional reimbursement vouchers for experimental, development and production tooling expenses representing the proportionate amounts applicable to deliveries subsequent to August 1943 under its CPFF contracts. These vouchers, in the amount of $986,963.93 (Finding 24), represented all the remaining experimental, development and production tooling expense in the deferred account and applicable, under the reamortization plan, to CPFF production. At the time these vouchers began to arrive for audit in October 1943, defendant's Resident Auditor, Mr. Campbell, had been replaced by Mr. Ferris, and the Contracting Officer had been replaced by Captain Davies. Mr. DiLapo was still assistant auditor and he again urged that the expenses represented by the vouchers were not allowable items of cost under the CPFF contracts and should not be paid. His reasons were the same ones previously urged upon Mr. Campbell, and were apparently concurred in by his new superior as well as by a succeeding Resident Auditor, Mr. Leibman. At any rate, the auditors withheld certification of these vouchers.

In April and May of 1944, the Chief Cost Auditor for the General Accounting Office, Buffalo area, submitted to the Resident Auditor a series of "informal inquiries" relative to the previous payment of vouchers covering the $1,299,856.02 of experimental, development and production tooling expense. The General Accounting Officer excepted to such prior payments on the ground that because the deferred expenses had originally been amortized against fixed-price production contracts, "the status of the account [presumably the deferred account] at the time of the negotiations with respect to the estimated costs under his [the contractor's] contract

was such as to preclude consideration thereof as an existing 'Deferred' or 'Unliquidated' charge to the contract" (Finding No. 27). Following formal notices of exception and suspensions of the accounts of Col. Harris, the Finance Officer, issued by the Comptroller General of the United States in August 1944, the Finance Officer recouped the $1,299,856.02 previously paid to plain-
137 tiff by withholding from plaintiff sums totaling that amount which were otherwise due plaintiff.

In the meantime, plaintiff's last series of vouchers, submitted in 1943, and covering the balance of its experimental, development, and production tooling expense in the amount of $986,963.93 had not been acted on by the Contracting Officer. On January 10, 1945, Captain Davies, as Contracting Officer, rendered findings of fact and a decision on these vouchers adverse to plaintiff. On March 1, 1945, Captain Davies rescinded his prior decision and forwarded new findings of fact and a decision (Finding No. 30). The two documents were substantially the same and both concluded that the items of expense covered by the vouchers were not allowable costs under the CPFF contracts and would not be reimbursed. Pertinent details of these two decisions will be discussed hereinafter.

On March 27, 1945, plaintiff appealed the findings and decision of the Contracting Officer to the War Department Board of Contract Appeals and on April 29, 1946, that Board rendered its decision in which it denied plaintiff reimbursement of the sum of $986,963.93. Plaintiff's application for a rehearing was denied by the Board on May 31, 1946.

We shall first consider defendant's administrative defenses. These defenses are, (1) that plaintiff failed to exhaust the administrative remedies provided for in its contracts with respect to the $1,299,856.02 of its claim which was originally paid to plaintiff and later recouped by defendant from money otherwise due plaintiff, and (2) that the decision of the Board of Contract Appeals, adverse to plaintiff with respect to its right to reimbursement for the balance of its claim ($986,963.93), was final and binding on the parties and therefore not reviewable by this court.

Alleged failure of plaintiff to exhaust its administration remedies

Plaintiff's claim falls in two parts for the purpose of defendant's administrative defenses. That part which is the target of the above defense is the $1,299,856.02, representing a por-
138 tion of the experimental, development, and production tooling expense carried in the deferred account and allocated, under plaintiff's revised books, to production of items under the CPFF contracts. Vouchers covering this amount were recom-

mended for approval by defendant's Resident Auditor, approved by the first Contracting Officer, and paid by defendant's Finance Officer in 1943. Subsequently, the General Accounting Office came to the conclusion that the CPFF contracts did not authorize the allowance of such expenses as costs of performing the CPFF contracts, and the Comptroller General suspended the accounts of the Finance Officer who had made the payments to plaintiff. The Finance Officer immediately recouped the amount suspended by withholding from plaintiff an equivalent sum otherwise admittedly due plaintiff. Plaintiff has taken no steps to secure a reversal of the last action of the Finance Officer or to recover the amount withheld other than by bringing this action in court.

It is plaintiff's position that no administrative remedies were provided by its CPFF contracts against the recoupment; that the action of the first Contracting Officer in determining, under Article 3 (b) of its contracts that the amounts shown on the vouchers were allowable costs, was conclusive; that the decision of the Comptroller General, and that portion of the decision and findings of second Contracting Officer in March 1945, which purported to pass on the propriety of the action of the first Contracting Officer, were without effect; that no dispute ever arose under the Disputes article of the contracts concerning this matter and that plaintiff's only remedy lay in the Court.

Defendant's position is that Article 3 (b) of the CPFF contracts merely vests the Contracting Officer with *discretion* to determine allowable costs; that the approval of the vouchers by the first Contracting Officer under that article was purely *routine* and not conclusive nor binding upon the Government; that in any event a dispute did arise involving the sum covered by these vouchers and the recoupment of that sum, which was decided adversely to plaintiff under the Disputes article of the CPFF contracts by the second Contracting Officer in a decision dated March 1, 1945; that plaintiff did not appeal to the Head
139 of the Department from that portion of the findings and decision relating to such previously approved and paid vouchers, and that accordingly plaintiff has no standing in court with respect to that portion of its claim.

We cannot agree with defendant's contention that Article 3 (b) of plaintiff's CPFF contracts merely vested the Contracting Officer with discretion to determine allowable items of cost under T. D. 5000. That article does not say that the Contracting Officer *may* determine allowable items of cost in accordance with T. D. 5000. It says that the Contracting Officer *will* so determine the allowable items of cost. The contract article dealing with "payments" (Finding No. 20) provides that the Government *will cur-*

reatly reimburse the contractor for such expenditures made in accordance with Article 3 as may be approved or ratified by the Contracting Officer. These articles, we think, imposed upon the Government the duties of determining whether costs were allowable under T. D. 5000 and of approving them for reimbursement if they were.

We next turn to the effect of the determination made by the first Contracting Officer under Article 3 (b) that the $1,299,856.02 of experimental, development and production tooling costs evidenced by the vouchers, were allowable items of cost under T. D. 5000. First, we think that a determination made by a Contracting Officer under that Article, followed by actual payment to plaintiff, is conclusive and binding on the parties unless the contractor, being dissatisfied with the decision, makes an objection to it which would result in a dispute to be resolved by the means provided in the Disputes article of the contract. In the case of *James Stewart & Co.* v. *United States*, 71 C. Cls. 126, certain vouchers had been approved by the Contracting Officer under a CPFF contract between plaintiff and the Government, and the amounts shown on the vouchers were paid by the disbursing officers of the Government. The General Accounting Office, deeming the action of the Contracting Officer in approving the vouchers to have been erroneous, made certain disallowances to the amount of such vouchers in the accounts of the disbursing officers.

The Government then sought to recoup such amounts from
140 the contractor by means of a counter-claim against a judgment rendered by this Court in plaintiff's favor in another matter. The Contracting Officer had approved the payment of the vouchers under an article of the CPFF contract which provided in part as follows:

> *Cost of the work.* The contractor shall be reimbursed in the manner hereinafter described for such of its actual net expenditures in the performance of said work as may be approved or ratified by the contracting officer * * *.

The Government contended that the approval of the Contracting Officer under such article was not conclusive, and that upon a showing by the Government that the Contracting Officer was in any respect wrong in making his decision, the Government might recover. The court held that the decision of the Contracting Officer under the above quoted article of the contract was conclusive and was binding on the Government. *Judge Green*, speaking for the court, said, *inter alia:*

> If the decision of the contracting officer as shown by his approval or ratification was not final, his act in so doing was

merely an idle gesture, for the contention of defendant is that notwithstanding such approval it can raise any objection to these items that it sees fit. We do not think the contract can properly be so construed. In fact to so construe it would have the effect to strike from the contract the words "as may be approved or ratified by the contracting officer," for they become absolutely useless. * * * The actions of the parties * * * show very plainly that both parties considered that, subject to other provisions in the contract having no bearing on this particular case, the decision made by the contracting officer was final, and such would be the ordinary meaning given to the provision under consideration. It should also be noted in this connection that there is neither allegation nor proof of fraud, bad faith, or palpable disregard of the rights of either party by the contracting officer. So far as it appears from the evidence, he exercised the authority given him with an honest purpose to carry out the intention of the parties to the contract and his action was an exercise of the power conferred upon him by that instrument. He discharged that duty by the mutual assent of both parties. The terms by which the power was conferred and the duty imposed are clear and precise and they are susceptible of no other interpretation than that the action of the contracting officer in the matter of expenditures was
141 intended to be conclusive, in the absence of fraud, such gross mistake as would necessarily imply bad faith, or a failure to exercise an honest judgment. (pp. 129, 130).

In the instant case the Government does not claim that the record fails to show that the act of approval of the first Contracting Officer constituted gross mistake, or that his approval was secured by fraud on the part of the contractor. In its characterization of the approval as "routine", the Government does seem to imply that the Contracting Officer failed to exercise honest and independent judgment, but the record in the case does not sustain such a characterization. When these vouchers were presented for approval, the Contracting Officer first sought the advice and recommendation of the Resident Auditor and his staff. An assistant resident auditor was of the opinion that the expenses sought to be reimbursed as costs allowable under the contract, were in reality losses suffered by plaintiff on prior fixed-price experimental contracts and that the CPFF contract specifically provided against the allowability of such expenses as costs. This opinion was not concurred in by the Resident Auditor who recommended to the Contracting Officer that the vouchers contained

items properly allowable as costs under the contract. The Contracting Officer agreed with the opinion of the Resident Auditor and approved the vouchers for payment. This set of facts does not, we think, indicate a routine approval of the payment of such a large amount by the Contracting Officer, but rather an independent and honest exercise of his judgment. We accordingly conclude that the first Contracting Officer's decision under Article 3 (b) of the contracts approving the vouchers for payment, was in the circumstances of this case, conclusive and binding on the Government.

The action of the Comptroller General in suspending the accounts of the Finance Officer who had made the payments on the vouchers approved by the first Contracting Officer, and its opinion that the items covered by those vouchers were not allowable items of cost under the contract, did not have the effect of reversing the decision of the first Contracting Officer. As the Supreme Court said in *United States* v. *Mason & Hanger Company*, 260 U. S. 323:

142 Over the effect of these [decisions of the Contracting Officer] the Comptroller of the Treasury has no power. They were the acts and duty of the officer in charge, in the expression of which there was no ambiguity, and were, therefore, conclusive in effect (p. 326).

Next, we come to defendant's contention that a dispute under Article 16 of the contract arose which involved not only the unpaid vouchers for the balance of the deferred expense, but also involved the propriety of the first Contracting Officer's approval of the earlier vouchers, and also the matter of the Government's recoupment of the amount paid to plaintiff pursuant to those vouchers. The defendant says that the second Contracting Officer rendered findings of fact and a decision adverse to plaintiff, and that plaintiff, having failed to appeal to the Head of the Department from that portion of the decision relating to the decision of the first Contracting Officer and the recoupment, has failed to exhaust its administrative remedies under the contract and now has no standing in court as to those matters.

The findings of fact and decision of the second Contracting Officer, dated March 1, 1945, to which defendant refers, did purport to pass on the allowability as costs of the deferred expenses represented by the vouchers previously approved by the first Contracting Officer and paid to plaintiff by the Finance Officer, and also on the matter of the recoupment of a similar amount pursuant to the decision and suspension action of the General Accounting Office. Actually, we think, the only matter before the second Contracting Officer for decision on March 1, 1945, was the

allowability under the contract and T. D. 5000 of items of expense contained in a series of vouchers totaling $986,963.93, representing the balance remaining in Bell's deferred experimental, development, and production tooling account, and which had been allocated by Bell to production under the CPFF contracts. These vouchers began to arrive for audit in October 1943 but none of them were officially acted on until March 1, 1945. At about the time of the first presentation for audit of these particular vouchers, a new Contracting Officer had replaced the officer who had approved the previous series of vouchers, and a new resident auditor was also present on the job. The assistant resident
143 auditor who had recommended disallowance of the first series of vouchers, again made the same recommendation with respect to the second series, and his recommendation was ultimately accepted by the new resident auditor and the new Contracting Officer. In the summer of 1944, following informal inquiries initiated by the General Accounting Office into the payment of the first series of vouchers, and after the suspension of the accounts of the Finance Officer of a sum equal to the amount which had been paid to plaintiff under those vouchers, the Finance Officer recouped the amount suspended by withholding an equivalent amount from money otherwise due plaintiff. At that time, the second Contracting Officer still had taken no final action on the second series of vouchers. Apparently, on December 10, 1943, the resident auditor on the Bell job had written to the District Auditor, Eastern Procurement District, under a subject heading "Amortization of Losses on Fixed Price Contracts," and covering Bell's treatment of the entire amount of experimental, development, and production tooling expenses carried in the deferred account. On January 20, 1944, the Eastern Procurement District forwarded the letter of December 10, 1943, and all subsequent correspondence on the matter, to the Chief of the Procurement Division for his views "as to the right of Bell to be reimbursed under its CPFF contracts for any portion of the said amount." On November 13, 1944, the Chief of the Procurement Division wrote to the District Supervisor of the Eastern Procurement District reviewing in general the facts concerning the deferred account and Bell's handling of the account, and expressing the opinion that the amount of such expense which Bell had allocated to the CPFF contracts did not, in fact, represent costs of performing such contracts, and concluding as follows:

> It is therefore the opinion of this Headquarters that Bell is not entitled to reimbursement under its CPFF contracts for P-39 and P-63 airplanes for any portion of the said sum of $2,286,819.95.

The sum so mentioned included both the amount covered by the vouchers approved by the first Contracting Officer and paid to plaintiff, and the amount covered by the second series of vouchers which were before the second Contracting Officer for approval.

144 On January 10, 1945, the second Contracting Officer wrote to plaintiff stating that he was forwarding a copy of the above-mentioned decision of the Chief of Procurement on the reimbursement of amortization of development and experimental expense over CPFF contracts, and that the Contracting Officer was incorporating that decision as his findings of fact "in denying reimbursement to the contractor for this expenditure, as requested on Audit Bureau Vouchers as follows:". The Contracting Officer then listed the unpaid vouchers totaling $986,963.93. On March 1, 1945, the Contracting Officer wrote to plaintiff again stating that the findings of fact and the decision which he had rendered on January 10, 1945, were rescinded and new findings and a decision were being forwarded. The new findings began with a listing of the identical unpaid vouchers, and continued almost word for word in the same manner as previously, except for the omission of the first paragraph of the prior findings which had related to the circumstances under which the Chief of Procurement Division was rendering advice, and a change in the last sentence of the "findings" to make it read, "It is, therefor, the decision of the Contracting Officer" rather than "It is therefore the opinion of this Headquarters."

The November 13, 1944, letter from the Chief of Procurement, was merely an expression of the views of that office on the question of the reimbursability of deferred experimental, development, and production tooling costs under plaintiff's CPFF contracts. That letter discussed the problem generally and referred to the entire amount in the deferred account and to the vouchers previously approved and paid, as well as to the subsequent series of vouchers which were before the Contracting Officer for approval. The Contracting Officer, for some reason, adopted this letter (as pointed out above) as his findings of fact and decision, but since the only matter actually before the Contracting Officer for decision was the approval or disapproval of the second series of vouchers, the findings and decision of the Contracting Officer are without any effect on plaintiff insofar as they related to vouchers other than the second series actually before him. In its subsequent and timely appeal from this decision to the Board of Contract Appeals for the War Department, plain-

145 tiff referred only to the second series of vouchers which had been disapproved, and the Board confined its decision to the matter of the disallowance of those particular vouchers.

In our opinion, plaintiff was not obliged by its contract to take an appeal from that portion of the second Contracting Officer's decision which purported to pass on the matter of the prior approval of the first series of vouchers, or on the matter of the recoupment. The decision of the first Contracting Officer had been favorable to plaintiff and no dispute arose over his decision which called into play the provisions of the Disputes article. Further, there was no occasion for the second Contracting Officer to make any findings or render any decision with respect to such prior decision of the first Contracting Officer. Plaintiff had nothing to appeal from with respect to the decision of the first Contracting Officer and the contracts afford the Government no right of appeal from that decision. The Government's only recourse, if it disagreed with such a decision, was to effect recoupment if possible, and, in the event of a lawsuit, attempt to show that because of some vital circumstance, the decision of the first Contracting Officer had been robbed of its usual conclusiveness.

The subsequent recoupment of an amount equal to that covered by the first vouchers which had been approved and paid, was not a matter which plaintiff was bound to appeal to the head of the department under any provision of its contract. If anything, it was a matter which plaintiff might consider a breach of the Government's contractual undertaking to pay sums admittedly due, and was the proper subject of a lawsuit.

We conclude that plaintiff has not failed to exhaust its administrative remedies with respect to the first series of vouchers or the recoupment of the amount paid under such vouchers. Furthermore, inasmuch as the defendant has failed to point to any circumstance which would defeat the conclusiveness of the decision of the first Contracting Officer, and since the General Accounting Office was without the power to reverse such decision, plaintiff is entitled to recover the amount approved for payment, paid and subsequently recouped, in the sum of $1,299,856.02.

146 *Finality of the decision of the War Department Board of Contract Appeals*

That portion of the second Contracting Officer's findings and decision of March 1, 1945, which dealt with the allowability as costs of $986,963.93 of deferred experimental, development, and production tooling expense, was duly appealed by plaintiff to the War Department Board of Contract Appeals and that Board decided that such items of expense were not reimbursable under plaintiff's CPFF contracts.

Defendant says that pursuant to the Disputes articles in the CPFF contracts, the decision of the Board was final and that no appeal therefrom lies in the courts. The Disputes article appearing in each of the contracts is the usual one in the standard form of Government contracts, and provides that, except as otherwise specifically provided in the contract, all disputes concerning questions of *fact* arising under the contract, not disposed of by mutual agreement, shall be decided by the Contracting Officer in writing; that such decision may be appealed by the contractor within 30 days to the Secretary of War or his designated representatives, whose decision thereon shall be final and conclusive upon the parties thereto (Finding No. 20).

It is plaintiff's position that the decision of the War Department Board of Contract Appeals is not binding on this Court because the Board's conclusion concerned a question of law and not of fact, but that if the Court should consider the question to be one of fact, then the Board's conclusion is not binding because it is arbitrary and capricious and directly in conflict with its own primary findings of fact.

Defendant contends that the question in dispute and decided by the Board was one of fact and not one of law. Defendant points out that the Contracting Officer had found as a fact that the sum in question "which plaintiff had charged on its books against CPFF contracts does not, in fact, represent costs of performing such CPFF contracts." Defendant urges that by dismissing plaintiff's appeal, the Board was, in effect, sustaining that finding of fact.

In its decision the Board set forth the facts concerning plaintiff's deferred account and its fixed-price and CPFF
147 contracts, much as we have done in our findings of fact herein. The Board stated that there was no dispute between the parties as to the amount of the costs involved, nor as to the propriety of the plaintiff's method of allocation; that the CPFF contracts provided that allowable items of cost were to be determined by the Contracting Officer in accordance with the pertinent provisions of T. D. 5000; that the experimental and development costs in question were clearly within the category of indirect costs as defined by T. D. 5000 and were specifically covered by Section 26.9 (d) thereof; that the production tooling covered by the deferred production tooling costs were used in the performance of the CPFF contracts; that such items of cost were within the intent and meaning of T. D. 5000, specifically, Section 26.9 (e) (5) (D) (Finding No. 31). The Board then stated, however:

> Although it is true that costs of this type may properly be allowed as reimbursable items under T. D. 5000, it does not follow that such costs *must* be reimbursed under T. D. 5000 in all cases and *under all circumstances*. In order to determine whether such items of costs should be reimbursed it is necessary to examine all of the circumstances and facts involved. [Italics supplied.]

The Board then referred to the fact that plaintiff had originally planned to amortize all such expense over a fixed-price contracts only; that after entering into the CPFF contracts, plaintiff had changed its plan of amortization in accordance with the position taken by the Bureau of Internal Revenue and the Renegotiation authorities, and had revised its books to spread the amortization over *all* its contracts for production of the P-39 airplane, both fixed-price, and cost-plus. The Board concluded as follows:

> Under these circumstances, it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated appellant did not intend that the item should be reimbursable and was in fact charging the costs in question against other contracts in accordance with a previously adopted plan. * * * Under the circumstances here present, the Board is of the opinion that the costs are not reimbursable under the subject contracts.

148 In making the above statement, we think the Board had reference to the language in T. D. 5000, Sec. 26.9 (d) which states that "upon a complete showing of all pertinent facts [these costs] are properly to be included as a cost of performing the contract * * *." Accordingly, the Board held that the circumstance of plaintiff's not having originlly intended to allocate any portion of such costs to the CPFF contracts was one of the circumstances contemplated by the contract (T. D. 5000) as foreclosing reimbursement of this type of cost, otherwise reimbursable. This was not, we think, a conclusion that the items in question were not "costs of performing such CPFF contracts." Without going into the merits of whether this was the sort of circumstance or "pertinent fact" contemplated by Section 26.9 (d) of T. D. 5090, we think that the Board's decision on whether, under the circumstances here present, the contract required reimbursement, involved an interpretation of plaintiff's CPFF contracts. That the Board itself so viewed its decision is indicated by the following language in its decision:

> There is no dispute between the parties as to the amount of the costs or as to the propriety of the method of allocation used by appellant. The only question presented is whether reimbursement for any portion of these costs is authorized or required by the subject contracts under the circumstances here involved.

In the case of *Wunderlich* v. *United States*, 117 C. Cls. 92, we pointed out that the distinction between questions of law and questions of fact is not always a clear one, but that in general the courts have held that questions of the interpretation of contracts are not "questions of fact" within the meaning of that expression as it is written into the Disputes articles of Government contracts. *McWilliams Dredging Company* v. *United States*, No. 48894, decided June 5, 1950, and cases cited therein. In its decision in the *Bell* case, the Board of Contract Appeals noted that the contracts all contained the standard "Disputes" article which referred only to decisions on questions of fact. The Board then stated:

> Insofar as the questions presented by this appeal are questions of law they will be administratively determined pursuant to the memorandum of the Secretary of War dated 4 July 1944.

149 That Memorandum gave the Board the following power, *inter alia:*

> (b) Consider and administratively pass on appeals not specifically or impliedly authorized by the contract where the ruling appealed from is not thereby made final and conclusive, and the appeal is taken within the time fixed in the contract for appeals.

The appeal in this case to the Board was from a decision of the second Contracting Officer that the items of expense involved were not allowable items of cost of performing the CPFF contracts, and also from his decision that such items were accordingly not reimbursable under the contracts. In his decision, the Contracting Officer made no reference to Article 3 of the contracts nor to T. D. 5000. In reviewing this decision, the Board carefully analyzed both the contract and T. D. 5000 and made findings not previously made by the Contracting Officer. The Board then concluded that the phraseology of the contract and T. D. 5000 made the items in question allowable items of cost,[4] but that certain circumstances, not

[4] To that extent the Board's ruling appears to be contrary to the ruling of the Contracting Officer.

specified in the contract or in T. D. 5000, but which, in the opinion of the Board, were contemplated therein, constituted a bar to reimbursement.

The decision of the Contracting Officer that the CPFF contracts did not permit reimbursement of these items was an interpretation of the contract and thus did not involve a question "of fact." The contracts themselves did not specifically nor impliedly authorize an appeal from such a decision, nor did the contracts make such a decision final and conclusive. In reviewing such a decision of the Contracting Officer, and in rendering its decision, the Board of Contract Appeals was only exercising the power defined in the Memorandum of the Secretary of War to consider and administratively pass on an appeal of this sort. Nothing in that Memorandum nor in the contracts, made the Board's decision on that question binding on plaintiff so as to preclude an appeal therefrom to the court. The Board might well have refused to exercise its discretion to render a decision in this case. In *Appeal of*
150 *Quipco Associates, Inc.*, (ASBCA No. 841, July 30, 1951), the Board had the following to say:

> The question as to what in fact was the subject matter of the contract of sale presents an issue which can be resolved only by a proper construction of the contract as a whole. Whether the contract, properly construed, contemplated identification of the subject matter of the sale by any words of description contained in the contract, or contemplated identification in some other manner such as by seller's display of the materials offered for sale, and whether or not Appellant is now entitled to any relief, including rescission, on the basis of the facts alleged, concerns essentially questions of law. * * * Any relief to which Appellant may be entitled could be granted only on the basis of a determination that as a matter of law the quoted provisions [of the contract], despite its phraseology, does not bar the granting of such relief. In that respect, also the dispute does not lie within the scope of the disputes clause * * * which is limited to disputes concerning questions of fact.

In some cases the Board has, as in the instant case, exercised its discretion to administratively pass on a "question of law." In the *Appeal of Nash-Kelvinator Corporation* (NBCA 289, April 24, 1947) and in the *Appeal of Consolidated Vultee Aircraft Corporation* (NBCA 524, February 28, 1949) the Navy Board of Contract Appeals had before it questions similar to the one in suit, i.e., whether under CPFF contracts the contractor was entitled to reimbursement as allowable costs, of a properly allocated portion of certain contributions made to local charitable organizations. The Board in each case stated that it was considering the appeal

pursuant to its directive from the Secretary of the Navy, which directive gave the Board *discretion* to consider and administratively pass on questions involving interpretations of contracts. In both cases the Board held that the contracts, properly interpreted, entitled the contractors to reimbursement for the contributions in question. In the *Consolidated Vultee* case, the contracting agency acquiesced in the Board's decision and requested payment be made to the contractor. The General Accounting Office, however, refused to permit payment and the contractor brought suit in the District Court (*Consolidated Vultee Aircraft Corporation* v.
151 *United States,* 97 F. Supp. 948). It is interesting to note that in the District Court proceeding, the Government's principal defense was that the Navy Board of Contract Appeals had no jurisdiction to decide *finally* whether an item of alleged cost was reimbursable under the CPFF contract because, under the Disputes article of the CPFF contract, its jurisdiction was confined to deciding questions of fact, whereas the question to be decided involved the interpretation of the contract, and, as such, was not a question of fact. The District Court did not pass on whether the question involved was one of fact or otherwise, and we mention the case only because in the instant controversy, involving an almost identical question, the Government is contending that the question is one of fact.

There is no doubt in our minds that the question decided by the War Department Board of Contract Appeals in the *Bell* case involved the interpretation of the CPFF contracts and the question was therefore not one of fact. Accordingly, an adverse decision of that Board did not bar plaintiff from bringing an appeal therefrom to this Court.

We now turn to the parties' position concerning the merits of the controversy on the law and on the facts.

Defendant says that the deferred experimental and development expenses are not properly allowable costs because in reality they were losses suffered by plaintiff in the performance of its fixed-price experimental contracts in 1936, 1937 and 1938 and that their reimbursement is specifically forbidden by Section 26.9 (g) (4) of T. D. 5000 which reads in part as follows:

> * * * Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such cost, are the following: * * * losses on other contracts; * * *

It is true that the bulk of the expenses in question contained in the deferred account were incurred in the performance of the experimental contracts with the Government, although a portion of them were incurred by plaintiff in the course of further research

after completion of the experimental contracts. It is also true that the contract price agreed to and paid by defendant on each experimental contract was much less than the actual cost to plain-
152 tiff of performance.

In the performance of a *production* contract, if the cost of performing exceeds the sale price of the articles produced, such excess costs certainly represent a loss since the purpose of a production contract is to realize an amount in excess of all costs of production. However, in the performance of an experimental contract, the failure to realize therefrom an amount over and above the costs of performance does not necessarily result in a loss. Experimental and development costs are similar to organization expense or preliminary work in connection with any project or contract, the benefits of which will inure to an indefinite period or later operations. The benefit of such costs may well apply to later production, the extent of which might be indefinite or possibly unknown at the time the costs are incurred. Business prudence however, would preclude the deferment of any costs of this nature unless the management had reasonable grounds for believing that it would receive contracts or other business against which such costs might properly be amortized. Where there is reasonable expectation that the research and experimentation carried on in the performance of an experimental contract will be used in future production contracts, the costs in excess of the contract price paid for such experimental work are properly to be deferred and carried in the contractor's financial statement as intangible assets (sometimes referred to as temporary capital assets), although they may represent substantial costs incurred for designs, formulae, patterns and engineering tables having great value in the production of the type of product for which such designs and calculations were prepared. If the project for which such experimental and development expenses were incurred were completely abandoned and an entirely new venture pursued, then these deferred costs would be determined to have no inherent value or benefit to later production and would be charged off to the company's surplus account
153 even though a deficit would result.[5] However, where the company secured production contracts for items directly related to the experimental work, the deferred intangible assets are usually and properly amortized and written off against such production so that the financial statement of the company will be void of items of an indeterminable value. The period of amortization may be indefinite and will depend largely upon the prospects

[5] In the instant case, for example, if plaintiff had diverted its attentions and efforts to the production of ships, tanks or automobiles to which its experimental and development work would have no application, it would have been improper for plaintiff to have deferred such costs for application against later production.

of volume production which would benefit by the deferred costs previously incurred.

In plaintiff's case, the demand for fighter planes was greater than production capacity. As early as 1938 plaintiff was reasonably sure that future production contracts would result from its experimental work on the fighter planes, and it commenced to defer its experimental and development expense. The war in Europe started in September 1939 and during that year plaintiff received its first production contract (a fixed-price contract) for approximately 87 P-39 fighter planes. At the end of 1939 and the end of 1940 plaintiff deferred additional costs which it incurred in the course of further experimental and development work for this type of plane. Other production contracts for the plane were received in 1940 which assured increased production of this type of plane.

In view of the continuity of the demand and the war engagements of the United States, it was reasonable and proper for plaintiff to extend the period of amortization against performance of production contracts which it received from time to time after 1940. Since the production contracts contained adequate provisions for compensation in case of termination for the convenience of the Government, it was also proper to include the total number of planes specified in such contracts as a basis for prorating the amortization of the experimental and development costs. Plaintiff could, within the limits of any possible corporate charter restrictions, have amortized these intangible capital assets over part or all of the production contracts directly related to the experimental work which created the assets. Inasmuch as all the items produced under the contracts were so related, it was the best practice to carry out the amortization over all such contracts since such experimental expenses were truly an element of the cost of producing each item called for by such contracts.

154 The terms "costs" and "losses" are not synonymous, and in the case of experimental projects which lead to profitable production contracts, the excess of costs of the experimental work over the price paid for such work, represents a temporary or intangible capital asset and not a loss. In plaintiff's case, the experimental and development work which it had done led to its receiving very large production contracts, and the products so manufactured embodied benefits which derived from the prior experimental work. Therefore the costs incurred in the latter would in no sense be considered losses, notwithstanding the fact that the actual costs of the experimental work were not fully recovered under the experimental contracts.

We accordingly conclude that the prohibition against inclusion as costs of performance in production CPFF contracts of losses

sustained on other contracts (T. D. 6000, Sec. 26.9 (g) (4)) does not apply to these experimental and development costs.

Next, defendant contends that the production tooling expenses carried in the deferred account were not actually a part of the cost of production under the CPFF contracts. Production tooling was commenced in 1939 and increased in volume as plaintiff received additional production contracts during 1940. Although plaintiff had received fixed-price contracts for approximately 1,600 planes by October 1940, only a small portion of deliveries were completed under these contracts by the end of 1940. Accordingly, it was proper for plaintiff to defer the tooling cost for the performance of these contracts and allocate such costs to deliveries in later years.

The CPFF contracts called for the same type of fighter plane for which the tooling had been provided in the performance of the fixed-price contracts. Thus, the tooling provided for the fixed-price contracts was utilized, with replacements from time to time, in the production of the same type of plane under the CPFF contracts. To the extent the performance under the CPFF contracts utilized the original tooling or replacements thereof, the original costs became properly applicable to performance under the CPFF contracts. Part of the original tooling became worn out or
155 obsolete during production on fixed-price contracts and had to be replaced. The cost of replacing tools was charged currently to production on fixed-price contracts, so that when the work was started on the CPFF contracts, the value of the original tooling was substantially the same as its original costs. Then, when these tools were scrapped due to a later change in model, the proceeds of the sale of such tools or scrap was credited entirely to the Government under the CPFF contracts. We conclude that a portion of the production tooling exepnse carried in the deferred account was properly a part of the cost of producing the planes under the CPFF contracts.

Next, the defendant says that if the Court should hold, as we do, that plaintiff's deferred experimental, development, and production tooling costs were actually a valid part of the cost of producing each item under both the fixed-price and the CPFF contracts, plaintiff still cannot recover because the Government did not in fact agree in the CPFF contracts that such costs would be reimbursed. Defendant bases this conclusion on the fact that until 1943 it had been plaintiff's intention to amortize *all* such costs over its fixed-price production contracts only and that plaintiff in fact did so; that it was not until the Bureau of Internal Revenue and the Renegotiation authorities of the Government insisted that such an allocation improperly reduced plaintiff's actual profits on its fixed-price contracts; that plaintiff reallocated such

deferred costs to all production, including production under its CPFF contracts; that these costs were not included in plaintiff's original negotiations for the CPFF contracts, but that they were included in plaintiff's bids on the fixed-price contracts; that reimbursement of this type would be contrary to the intentions of the contracting parties as shown by all the facts.

The intention of the contracting parties may become important and perhaps controlling in the interpretation of a contract where the language of that contract is ambiguous and not clear. In the instant case Article 3 (b) of the CPFF contracts provided that allowable items of cost would be determined by the Contracting Officer in accordance with "Regulations for determination of the cost of performing a Contract as promulgated by the Treas-
156 ury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940." Section 26.9 (c) (5) (D) quoted both in Finding No. 19 and earlier in this opinion, provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. The deferred charges for production tooling clearly fall within this category of factory costs. Section 26.9 (d) also quoted in Finding No. 19 and earlier in this opinion, specifically provides that deferred experimental and development charges "upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract." There is nothing ambiguous about the language of the contract or T. D. 5000 regarding the treatment the parties agreed would be accorded to the charges in question. It appears to be defendant's position, however, that certain "pertinent facts" present in this case prevent the treatment of these charges as items of cost of performing the contract at least for the purposes of reimbursement.

There is no real dispute between the parties as to the existence of most of the "pertinent facts" relied on by the Government: that the costs were incurred several years prior to the entry into the cost-plus contracts; that in the course of the CPFF negotiations plaintiff had not intended to allocate any of such charges to production under the CPFF contracts and did not include any part of such charges in its costs estimates. What, then, is the significance of those facts on the question of plaintiff's right to reimbursement?

That the expenses were incurred several years prior to the entry into the CPFF contracts is, we think, immaterial, since the charges were incurred and properly deferred in the expectation that the experiments would lead to profitable production contracts for the manufacture and sale of articles to which the research and develop-

ment would apply, and the CPFF contracts in question represented a portion of the fulfillment of that expectation. The production tooling, although used for production under the fixed-price contracts, was also used for the CPFF production and could not be used for producing other types of planes.

157 Plaintiff did not, at the time it was negotiating for the CPFF contract, intend to allocate any of its deferred experimental, development, and production tooling expenses to the CPFF contracts, and in its estimate of costs which it was required to make and present to the Government in negotiating the CPFF contracts, plaintiff did not include any amount to cover costs of this type. The contract itself provides for the consequences of such an omission from a contractor's cost estimates in Article 3 (a) as follows:

> The Government will pay the Contractor upon satisfactory delivery of all items specified in this contract, subject to reimbursements for cost, as outlined in Article * * * hereof, the cost, plus a fixed fee of * * * Dollars and * * * cents * * * being * * * percent * * * of the total estimated cost of * * * Dollars * * *. This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article * * * herein, provided, however, that there shall be no adjustment of the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

Plaintiff omitted the items of expense in question from its estimated cost upon which its fixed fee was based and that omission would be a complete defense to a claim by plaintiff for an increase in its fixed fee. But plaintiff is not seeking an increase in its fixed fee and nothing in Article 3 indicates that a legitimate item of cost may not be reimbursed merely because it was omitted from the original cost estimates.

The omission of these expenses from cost estimates was intentional on plaintiff's part and was apparently communicated to defendant. However, it has not been shown that defendant relied on plaintiff's intention not to request reimbursement and because of such reliance changed its position so as to work an estoppel. The record merely indicates that some agent of defendant had expressed the opinion to plaintiff, prior to the execution of the CPFF contracts, that experimental, development, and production tooling expenses would not be reimbursable, and that plaintiff accordingly

decided not to request reimbursement. This understanding,
158 if any, was not expressed in the contracts ultimately entered into, although it might easily have been done by expressly excluding such items in the contract. A similar situation existed in the *Appeal of Nash-Kelvinator Corporation*, NBCC 289, a case decided by the Navy Board of Contract Appeals on April 24, 1947. In that case the dispute involved the reimbursability of certain charitable contributions expressly made reimbursable under paragraph 40 (f) of Explanation of Principles for Determination of Costs under Government Contracts, a document relative to costs similar to T. D. 5000, and incorporated by reference into the CPFF contract. On the basis of a departmental expense ruling and a decision of the Comptroller General, the Navy Department denied reimbursement. In holding for the contractor, the Board stated:

> Had it been the intention of the Government to exclude contributions of the character described in paragraph 40 (f) from allowable costs, the obvious means of achieving such exclusion would have been the omission of paragraph 40 (f) and the express exclusion of such expenses.

See also *Todd Shipyards* v. *United States*, (No. 48916) decided by this court on November 7, 1950.

As to defendant's contention that plaintiff had included all these deferred costs in its estimates used in bidding on the fixed-price production contracts, the Commissioner has found (Findings No. 12 and No. 41) and we have adopted his finding, that plaintiff did not include such costs in its bid estimates. At the time plaintiff was bidding on the fixed-price production contracts executed in 1939 and 1940, (Finding No. 9 for dates of execution of those contracts), only a portion of plaintiff's experimental and development costs had been determined and set up in the deferred account, and the production tooling expense involved herein had not yet been determined inasmuch as that expense grew largely out of the performance of those fixed-price production contracts. In any event, we do not believe that the inclusion or exclusion by plaintiff of these costs in its bid estimates would have any bearing on the issues of this case. It is our understanding that in making a bid, a fixed-price contractor usually tries to arrive at a price sufficiently low to secure the award, but high enough to secure a profit. In
159 figuring a bid and in performing the contract, the cost problem as such, is one for the contractor. His contract protects him from increased costs clearly due to changed conditions or changes brought about by Government action, and the Government, in turn is protected from improper allocations of cost by the Renegotiation Act. Regardless of how much of the instant costs were

actually included in the fixed-price bid estimates, plaintiff did attempt to allocate all of these costs when determined, to its fixed-price contracts, whereupon the Government proceeded, under the Renegotiation Act, to protect itself by disallowing a portion of the costs in the computation of plaintiff's profits for renegotiation purposes in 1942.[6]

We conclude that plaintiff's intention not to allocate any part of the costs in question to its CPFF contracts and its omission of such costs from the cost estimates submitted to defendant in negotiating such CPFF contracts, are not "conditions" or "pertinent facts" which makes those costs non-reimbursable under the CPFF contracts. The actual omission is significant only for the purpose of computing plaintiff's fixed fee, and the amount of such fee is not involved herein. The contracts as entered into all expressly provided that such costs would be reimbursed. Plaintiff was under no contractual obligation to request reimbursement for any particular costs, but the contracts did obligate the Government to reimburse plaintiff for any costs made reimbursable by the contracts if, as here, reimbursement was requested.

In its defenses to the merits of plaintiff's claim, defendant makes the same argument urged earlier in the administrative defenses, that the contract and T. D. 5000 made the Contracting Officer's determination of allowable costs merely discretionary. We have already decided that the language of Article 3 (b) imposes upon the Contracting Officer the obligation to determine whether or not costs are allowable under T. D. 5000. The use of the word "may" in the latter part of Section 26.9 (d) of T. D. 5000 does not weaken that obligation as a reading of the whole section will demonstrate.

Defendant also contends that in order that deferred or capitalized experimental and development expenses be reimbursable as
160 costs, they must have been amortized in accordance with a reasonably consistent plan. Defendant urges that plaintiff, in extending the amortization of the costs of experimental work over the production under CPFF contracts instead of confining such amortization to production under its fixed-price contracts as previously planned, had, in fact, two plans of amortization and that these plans were inconsistent. Plaintiff's basic plan of amortization (Finding No. 14) was to amortize these expenses over future production of products utilizing the designs and plans developed and this, in fact, is what plaintiff dd. There was never any change in that basic plan. Both the Board of Contract Appeals and this Court have found that the amounts requested by plaintiff for reim-

[6] The terms of the settlement agreement ultimately entered into by the parties, are discussed elsewhere in this decision.

bursement represented a proper proportion of such deferred expense determined by "a ratable allocation which is reasonable in consideration of the pertinent facts."

Defendant further contends that the charges in question are not allowable items of cost because T. D. 5000 contemplated reimbursement only of "*unliquidated* experimental and development charges." It is defendant's position that these charges were completely liquidated under plaintiff's first plan of amortization against the fixed-price contracts by the end of 1942. Section 26.9 (d) which describes "other manufacturing cost" properly includable as a cost of performing the contract, mentions "deferred" or "unliquidated" experimental and development charges. As an explanation of what is meant, the section states:

> For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract.

At the time plaintiff presented its first vouchers for reimbursement of these charges, plaintiff had completely revised its books back to 1940, so that only that portion of its deferred charges ratably allocable to production under the fixed-price contracts had been amortized. The amount of experimental and develop-
161 ment charges for which reimbursement was requested on the vouchers was still carried in the deferred account and met all the tests of Section 26.9 (d). Neither the Bureau of Internal Revenue nor the Government Renegotiation Authorities considered these deferred charges actually or irrevocably "amortized" or "liquidated" by plaintiff's previous bookkeeping entries which had charged them all off to production under the fixed-price contracts. In their opinion, no amount of bookkeeping could alter the actualities of the situation, i.e., that these deferred charges were properly costs of every plane produced which utilized the designs, experimentation and production tooling represented by such charges. By the time plaintiff submitted its vouchers under the CPFF contracts, it had changed its bookkeeping to reflect the true state of affairs.

Our discussion above relates in part to another contention urged by defendant, namely, that to allow plaintiff to be reimbursed for the deferred charges properly allocable to production under the CPFF contracts, woud in effect be to pay plaintiff twice for the same thing. This "double payment" argument seems to be based on the theory that because plaintiff made a profit on its fixed-price

production contracts sufficient to cover all of the deferred charges, those charges were automatically written off or "liquidated". Plaintiff has pointed out exactly where such an argument could lead. For example, if plaintiff had, in fact, suffered losses on the fixed-price contracts, which losses exceeded in amount the total of the deferred charges, and plaintiff had elected to amortize none of those deferred charges over such fixed-price contracts, then, under defendant's theory, all of the deferred charges would be allowable items of cost reimbursable under the later CPFF contracts, since there had been no profits from the fixed-price contracts to affect the "liquidation" of those charges. It is obvious from the language of Section 26.9 (d) of T. D. 5000 that such an allocation of all deferred charges to a CPFF contract where a portion of them represented the cost of producing items under other contracts, was not contemplated and would not have been permitted. Regardless of profit or loss resulting from production contracts, the deferred charges represented a portion of the cost of every plane produced under such contracts and plaintiff's revised books so treated the deferred charges.

162 Defendant suggests that the Government received nothing of value that it would not have received under the original conditions as they existed at the time the CPFF contracts were negotiated, and that plaintiff incurred no expense that it would not have incurred had no CPFF contracts been made by it with the Government. By the expressin "under the conditions as they existed", defendant apparently is referring to the then state of plaintiff's bookkeeping which had allocated all of the deferred charges to the fixed-price contracts. As we have stated previously, a proper portion of those deferred charges were elements of cost of producing planes under the CPFF contracts regardless of plaintiff's books, and had the experiments not been conducted and the charges not incurred, defendant could not have secured any of the planes from plaintiff. The fact that the expenses were incurred prior to the entry into the CPFF contracts does not prevent a portion of those expenses from being costs of manufacturing planes under those contracts, as T. D. 5000, Section 26.9 (d) expressly provides. As for the deferred production tooling expenses which plaintiff had originally amortized against fixed-price contracts only, plaintiff's bookkeeping and its original intentions regarding amortization do not alter the fact that those production tools were used in producing the CPFF planes and a certain portion of those deferred charges were actually a part of the cost of such production.

Finally, defendant says that if the Court should hold that the deferred charges in question constitute allowable items of cost under the CPFF contracts which should have been reimbursed, then only

the excess costs in the sum of $229,986.30 which had been allocated by plaintiff to the experimental "Airacobra" contract should be charged off against subsequent P-39 production. Defendant urges that plaintiff has not shown that the balance of the deferred experimental and development charges, allocated to the Airacuda and the Airbonita experimental work were of benefit in the P-39 production.

As pointed out in our Finding No. 6, all excess costs on experimental contracts were classified as experimental and development expense and were accumulated from year to year during the performance of the several experimental contracts. No
163 segregation of these costs was made as to their application to the specific contracts on which excess costs were incurred except the first amount deferred in 1938 which resulted from work on the experimental contract for the Airacobra. Plaintiff's auditors made an approximate allocation of this expense to the three experimental contracts by deducting from the costs of fulfilling each contract, the income received, and under that allocation (set out in Finding No. 6) the approximate allocation to the Airacobra was $229,986.30. Actually, no reasonably correct segregation of costs to any particular experimental contract had been possible since the improvements in design and fabrication developed in earlier operations were carried forward and applied on later experimental and development work on other models and finally into production contracts. The costs thus represented deferred values of designing and experience in fabrication rather than costs of any particular experimental airplane contract. In Finding No. 36 there are described some of the basic principles of design and fabrication which plaintiff developed on its experimental contract work and incorporated into the P-39 production models. Most of the developments, engineering standards and fabricating processes acquired during the performance of all three experimental contracts were incorporated and utilized in all subsequent production. The few developments not specifically utilized in the planes produced were of value because of the engineering knowledge gained that the particular design or development was not entirely satisfactory. The Commissioner has found, and we have adopted his finding, that the true measure of the value of the experimental work on all three models to production of planes after 1940 is represented by the excess of costs on the experimental contracts over and above recoveries under these contracts in the net amount of $1,499,739.23, and that sum is thus the fair and reasonable value of the general experimental and development work in benefits and savings on the later production contracts.

Under the clear provisions of plaintiff's CPFF contracts and T. D. 5000, a portion of plaintiff's deferred experimental, develop-

ment, and production tooling expenses were allowable items
164 of cost and should have been reimbursed. The portion sought to be amortized against the CPFF contracts and claimed as allowable costs subject to reimbursement (Finding No. 41) represents a reasonable allocation of such costs on the basis of all production contracts. The sum so allocated is $2,286,819.95 and plaintiff may have judgment for that amount.[7]

It is so ordered.

WHITAKER, *Judge;* and LITTLETON, *Judge;* concur.

JONES, *Chief Judge*, dissenting in part:

I would disallow the second item of $986,963.93.

I agree that the Contracting Officer's decision was not necessarily final.

I would allow plaintiff to recover on the item which was paid and later recouped. This item had been approved by the Contracting Officer. Since it had been paid it manifestly had the approval of the other authorized officers of the Government. In the absence of fraud or mistake this should have been treated as final.

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[7] The matter of plaintiff's taxes and the final renegotiation settlement have been the subject of considerable discussion in this case. Neither matter is directly in issue or has a real bearing on plaintiff's right of recovery. The Bureau of Internal Revenue has already applied plaintiff's costs in the manner plaintiff is contending for herein. However, since these costs were denied as reimbursable costs under the CPFF contracts, the Bureau allowed these costs, on a pro rata basis, as deductions from the net fees that the plaintiff realized on its CPFF contracts for deliveries of planes during 1943, 1944, and 1945 (Finding No. 33). Had these costs been reimbursed by the Government under the CPFF contracts, the Bureau would not have allowed such costs as deductions from the fees collected. Accordingly, plaintiff's recovery of these costs herein will become taxable since they were allowed as deductions during 1943, 1944, and 1945.

The Bureau of Internal Revenue also allocated part of these costs to deliveries in 1942 both on fixed-price and CPFF contracts. But the profits on the fixed-price contracts during 1942 were much greater, and the entire year was subject to renegotiation by the War Department (Finding No. 32). However, the Renegotiation Board calculated plaintiff's profits on the original basis of charges for experimental, development, and production tooling costs amortized against plaintiff's fixed-price contracts only (Finding No. 16), disregarding the revision made by the Bureau of Internal Revenue. The amount of excess profits recouped by the Governmnt was thus less than it would have been if these charges had been allocated to all planes delivered and deliverable under all contracts then in force. Plaintiff was required to refund $7,714,000 on the basis of total and excess profits so determined, but the agreement provided that if the pro rata allocation sought by plaintiff was carried through and allowed on all planes delivered under the CPFF contracts, the 1942 charges for experimental, development, and production tooling expenses against fixed-price contracts would be reduced to the extent of such reallocation, and the excess profits recoverable under the renegotiation would be increased by $667,000 which plaintiff agreed to pay to the Government, less whatever tax credit plaintiff might be entitled to by so refunding to the Government this amount as excessive profits for 1942. The remaining sum would then become subject to further tax. All actual amounts must be calculated by the General Accounting Office in its ultimate settlement with plaintiff and plaintiff's settlement with the Bureau of Internal Revenue.

165 MADDEN, *Judge*, dissenting:

The War Department Board of Contract Appeals in its decision which is quoted in Finding 31 said:

> Under these circumstances, it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated appellant did not intend that the item should be reimbursable * * *.

The essence of this case is contained in the above statement. Is the plaintiff entitled to be paid $2,286,819.95 for something which, when it made the contracts under which it claims the payment, it intended that it should be paid nothing at all?

The plaintiff says that the contract, as written, calls for the payment, and that therefore it is entitled to it even though it did not count upon it or expect to get it, when it made the contracts. To bring about such a result, the contracts would have to speak in the plainest and most unmistakable language. But they did not do so. They spoke the language of T. D. 5000 which is quoted in Finding 19. In its paragraph (d) it says:

> For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract.

Before the cost-plus-fixed-fee contracts here in litigation were entered into, the plaintiff was following a method of amortization which would have completely written off these charges without attributing any of them to any future contract. After three of the four cost-plus-fixed-fee contracts were made, on August 14, 1941, September 10, 1941 and June 29, 1942, the plaintiff continued,
166 down to the end of 1942, to pursue the same system of accounting, and by that time had completely amortized all of the costs claimed in this suit. On September 19, 1942, plaintiff's treasurer wrote plaintiff's comptroller that it would be improper accounting to charge any of these expenses against cost-plus-fixed-fee contracts since, to make them reimbursable costs under those contracts, such costs "would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost-plus contracts in view of the position taken by the Government that prior to our entry into cost-plus contracts we have received sufficient fixed-price contracts to permit the

amortization of deferred experimental expenses." See Finding 22.

This statement of course referred to the position taken by the Government at the time the contracts were entered into. It certainly did not refer to the position taken currently by the Bureau of Internal Revenue of the Government, which was exactly the opposite. See Finding 21. And there is nothing in the record tending to indicate that there had been any discussion between the plaintiff and the contracting officers of the Government between the time that the contracts were negotiated and the time of the above-quoted communication, with regard to what should or should not be reimbursable. Finding 15 shows that the plaintiff set up its plan, limiting amortizatoin to its fixed-price contracts because it understood that the charges here in question were not to be reimbursable under its cost-plus-fixed-fee contracts.

The quoted statement of the treasurer puts beyond question the intention of the parties that the costs here sued for were not to be reimbursable. Their recovery is a complete and unexpected windfall of $2,286,819.95.

I have not failed to consider any equity in the plaintiff's favor which might arise from the fact that the change in the plaintiff's accounting method resulted from pressure which the Bureau of Internal Revenue put upon the plaintiff, in the Bureau's desire to establish a larger amount of excess profits made from the plaintiff's fixed-price contracts. As it turned out, the plaintiff's taxes for the years 1941 through 1945, during which it performed both the fixed-price and the cost-plus-fixed-fee contracts,
were increased only $32,056.17 over what they would have
167 been if they had been computed on the basis of the plaintiff's own method of accounting. As to the renegotiation of the plaintiff's contracts, the arrangement made was only tentative, and the plaintiff would not be prejudiced in that regard by an adverse judgment in this case.

The opinion of the Court accords finality to the Contracting Officer's approval of vouchers in the amount of $1,299,856.02, which were, accordingly, paid, and which are here in suit because that amount was subsequently recouped by the Government from amounts admittedly due the plaintiff under its contracts. I think the opinion of the Court is correct in not attributing to the plaintiff any failure to exhaust its administrative remedies in this regard. I think that the contract did not provide any administrative procedure which had to be followed, at the peril of losing a valid claim. But, on the other hand, I think that the provisions of Article 3 (b) of the contract, quoted in Finding 19, that "allowable items of cost will be determined by the Contracting Officer • • • " did not confer upon that officer the powers of an agreed

arbitrator such as are normally conferred upon that officer by Articles 4 and 15 of the usual Government contract. Article 3 (b) says nothing about finality and I would not be willing to decide that a cost-plus-fixed-fee contractor who was entitled to be reimbursed for an expenditure could be irrevocably denied reimbursement because the contracting officer, acting under Article 3 (b), had refused to approve the expenditure for reimbursement because he construed the contract erroneously. If such a question arose, and the contractor was dissatisfied with the amount paid him, I think he would have the right to establish his claim in this or some other competent court, without being prejudiced by an administrative decision which the court thought was wrong. For the same reason I think that the Government was not foreclosed by the erroneous decision of its Contracting Officer. He had no more power to give the plaintiff $1,299,856.02 which it had not contracted for than he would have had to deny the plaintiff that sum if it had been entitled to it under its contract.

I would dismiss the plaintiff's petition.

169 JUDGMENT OF THE COURT, OCT. 2, 1951

Upon the special findings of fact, which are made a part of the judgment herein, the Court concludes as a matter of law that plaintiff is entitled to recover.

IT IS THEREFORE ADJUDGED AND ORDERED that plaintiff recover of and from the United States the sum of two million two hundred eighty-six thousand eight hundred nineteen dollars and ninety-five cents ($2,286,819.95).

[Clerk's Certificate to foregoing transcript omitted in printing.]

17. SUPREME COURT OF THE UNITED STATES

No. ——, October Term, 1951

United States, *Petitioner*,

v.

Bell Aircraft Corporation

Order Extending Time to File Petition for Writ of Certiorari

Upon Consideration of the application of counsel for petitioner,

It Is Ordered that the time for filing petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including January 30, 1952.

Fred M. Vinson,
Chief Justice of the United States

Dated this 29th
day of December, 1951.

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1951

No. ——

THE UNITED STATES, *Petitioner*,

v.

BELL AIRCRAFT CORPORATION

STIPULATION AS TO PRINTING OF RECORD

Subject to this Court's approval, it is hereby stipulated and agreed by and between the attorneys for the respective parties hereto that for the purposes of petitioning for a writ of certiorari, the printed record shall consist of the pleadings, the findings of fact, conclusion of law, opinions and judgment of the Court of Claims, dissenting opinions by Jones, *Ch. J.*, and by Madden, *J.*, and the docket entries for the Court of Claims subsequent thereto.

It is further stipulated and agreed that the parties hereto may refer to the unprinted portions of the entire record which is being filed with this Court but which are not included in the proposed printed record herein.

PHILIP B. PERLMAN,
Solicitor General

WM. M. AIKEN,
Counsel for Respondent

January 17, 1952

☆ U.S. GOVERNMENT PRINTING OFFICE 1952—986372/P.O. 713

Supreme Court of the United States

No. 559, October Term, 1951

[Title omitted.]

Order allowing certiorari

Filed March 31, 1952

The petition herein for a writ of certiorari to the United States Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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986375—52——1

In the Supreme Court of the United States

BELL AIRCRAFT CORPORATION

No. 559

THE UNITED STATES, PETITIONER

v.

BELL AIRCRAFT CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the Court of Claims entered in the above-entitled case on October 2, 1951.

OPINION BELOW

The opinion of the Court of Claims (R. 101) is not yet reported.

JURISDICTION

The judgment of the Court of Claims was entered on October 2, 1951 (R. 135). On December 29, 1951, the Chief Justice extended the time for filing a petition for certiorari to January 30, 1952 (R. 136). The jurisdiction of this Court is invoked under 28 U. S. C. 1255 (1).

QUESTIONS PRESENTED

1. A standard provision in cost-plus-a-fixed-fee contracts provides that "allowable items of cost will be determined by the contracting officer" and contains no express language giving his determination finality. The question is presented whether that provision renders conclusive, and immune from judicial consideration, determinations of law, coming within its scope.

2. Whether, under the foregoing provision, the Court of Claims had any warrant for holding conclusive a decision of one contracting officer adverse to the Government as to allowable items of cost, while denying conclusiveness to a decision of a successor contracting officer in favor of the Government on the identical question.

3. Whether the Court of Claims erred in holding that the determination that certain claimed costs were not incurred incident to and necessary for the performance of the cost-plus-a-fixed-fee contracts was a determination of law which was not within the standard form provision that administrative decisions "on all disputes concerning questions of fact * * * shall be final and conclusive upon the parties * * *."

4. Whether, assuming the question was properly before it for decision, the Court of Claims erred in awarding reimbursement, under cost-plus-a-fixed-fee contracts, for items which the parties understood, when the contracts were

entered into, would not be claimed as reimbursable costs.

CONTRACT AND REGULATION PROVISIONS INVOLVED

The pertinent portions of the contract and regulation provisions are set forth in the Appendix, *infra*, pp. 19–24.

STATEMENT

This action arises out of respondent's claims for reimbursement of certain costs under four cost-plus-fixed-fee (CPFF) contracts with the United States. The Court of Claims' findings disclose the following pertinent facts:

In 1936–38, respondent received several fixed-price contracts from the Army Air Corps for the construction of certain experimental fighter planes (R. 67). The contract price agreed to and paid by the United States was insufficient to compensate respondent for the heavy experimental and development costs it had incurred under the experimental contracts (R. 69). Respondent accordingly deferred and capitalized these excess costs, amounting to $1,528,760.66[1] (R. 69).

In 1939–41, respondent entered into several fixed-price contracts with the Air Corps for the production of about 1,000 P–39 fighter planes at a cost of over 37½ million dollars (R. 71). During this period, respondent also entered into fixed-price contracts with the British Government for

[1] This was later adjusted to $1,499,739.23 after audit by the Army Audit Agency (R. 70).

the production of about 800 P–39's for almost 34 million dollars (R. 71).

The mass production of this large quantity of planes for the United States and Great Britain required respondent to incur production-tooling costs amounting to $1,894,109.57, which it deferred and capitalized[2] (R. 72). By the end of 1942, respondent had fully amortized all of these deferred production tooling costs and all of the deferred experimental and development costs against deliveries of the 1800 P–39 planes under its fixed-price contracts with the United States and Great Britain (R. 76).

In the meantime, starting August 14, 1941, respondent was awarded a series of CPFF contracts by the Air Corps for the production of over 10,000 additional P–39 planes at a total estimated cost of 307 million dollars plus a fixed fee of over 14 million dollars (R. 76–77). Three of the four contracts, calling for the production of over 5,000 planes, were entered into in 1941 and 1942, while respondent was still amortizing its experimental, development and tooling costs solely against the fixed-price contracts (R. 77). In the course of the negotiations for the CPFF contracts, it was understood by both parties that respondent did not intend to allocate any of the deferred costs against production under the CPFF contracts and there-

[2] This was later adjusted to $1,874,725.77 after audit by the Army Audit Agency (R. 72).

fore did not include any part of such costs in its cost estimates for those contracts (R. 82, 125).

In March 1942, the Bureau of Internal Revenue audited respondent's returns and required respondent, for tax purposes, to allocate the deferred experimental, development, and tooling costs to all P–39 production under both the CPFF contracts and the fixed-price contracts (R. 81).[3] Respondent refused to comply and, as already noted, continued to amortize the deferred costs solely against the fixed-price contracts until the end of 1942, when all the costs were fully charged off to the fixed-price contracts (R. 81–82). In September 1942, respondent explained this refusal to comply with the Bureau's requirement by stating that (R. 82):

> This item [deferred experimental, development and production tooling costs] should be allowed as an amortization expense against the fixed-price contracts only in view of the fact that any amortization to be allowable under a cost-plus-fixed-fee contract would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost plus contracts in view of the position taken by the Government that prior to our

[3] This reallocation would have resulted in higher profits under the fixed-price contracts and thereby increased respondent's income taxes for the years during which the fixed-price contracts were performed. However, as it turned out, respondent's tax liability was increased by only $32,056.17 because of the reallocation (R. 134).

> entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses.

In April 1943, respondent's comptroller submitted to the Air Corps a statement of accounting policies pertinent to the company's operations under the CPFF contracts, reiterating that the costs were chargeable only to fixed-price production (R. 82):

> Experimental, development and production tooling expenses are written off against the deliveries of the items to which expenditures apply. No experimental expense is charged to overhead applicable to CPFF contracts.

Six months later, however, respondent wrote to the Price Adjustment Officer in charge of renegotiation of respondent's contracts, proposing to reallocate its deferred charges as requested by the Bureau of Internal Revenue "provided that the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office" (R. 83). Upon approval of this proposal on September 9, 1943, by the Price Adjustment Officer for renegotiation purposes, respondent restored to the deferred account on its books a proportion of the experimental, development, and tooling expenses which it con-

sidered applicable to the CPFF contracts in accordance with the new plan of amortization (R. 84). The sum so restored amounted to $2,286,-819.95, the unrestored difference of $1,087,645.05 remaining applicable to the fixed-price contracts (R. 84–85).

Claiming that it was entitled to reimbursement under the CPFF contracts for the $2,286,819.95 so allocated by it, respondent submitted two sets of vouchers to the Air Corps for payment of that sum (R. 85). The first set of vouchers, allocated to deliveries under the CPFF contracts from 1942 to August 1943, and submitted in September 1943, amounted to $1,299,856.02 (referred to as the 1¼ million dollar claim) (R. 84–85). The second set of vouchers, allocated to deliveries under the CPFF contracts after August 1943, and submitted in October 1943, amounted to $986,963.93 (referred to as the $980,000 claim) (R. 85).

The Assistant Resident Auditor for the Air Corps recommended that the vouchers for the 1¼ million dollar claim be rejected on the ground *inter alia* that all of the costs had been charged off to the fixed-price contracts (R. 85). This recommendation was rejected and the vouchers were approved by the Resident Auditor for the Air Corps. They were also approved by the Contracting Officer and the 1¼ million dollar claim was paid to respondent by the United States, but later recouped after objection by the Comptroller General (R. 85, 87).

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The same Assistant Resident Auditor recommended rejection of the vouchers for the $980,000 claim for the same reasons he had recommended against the other claim (R. 86). By this time, the former Resident Auditor and the former Contracting Officer had been replaced. Their successors accepted the Assistant Resident Auditor's recommendation and declined to approve the vouchers for the $980,000 claim (R. 86, 88).

On March 1, 1945, the new Contracting Officer issued findings of fact on respondent's two claims, pointing out that the total of both claims, "the $2,286,819.95 which Bell had charged on its book against CPFF contracts did not, in fact, represent costs of performing such CPFF contracts," that "the costs in question were in fact recovered by [respondent] through the fixed-price contracts" and that "reimbursement for such costs under the CPFF contracts would result in Bell's receiving double payment from the Government" (R. 88–89, 91). The finding concluded that respondent was not entitled to reimbursement under its CPFF contracts "for any portion of the said sum of $2,286,819.95" (R. 89).

On respondent's appeal under Article 16 of the CPFF contracts (the general Disputes article) from that portion of the Contracting Officer's findings which denied the $980,000 claim, the War Department Board of Contract Appeals affirmed (R. 89–91). Respondent took no appeal from the Contracting Officer's denial of the 1¼

million dollar claim, which had theretofore been paid but recouped (R. 89).

Respondent then brought the instant suit in the Court of Claims, demanding payment of the 1¼ million dollar claim and of the $980,000 claim (R. 1–17). The court concluded that respondent was entitled to recover the full amount of both claims and awarded judgment for $2,286,819.95 (R. 101, 135). Chief Judge Jones and Judge Madden dissented (R. 132–133). Judge Jones agreed that respondent was entitled to recover on the 1¼ million dollar claim, but stated that he would disallow the $980,000 claim (R. 132). Judge Madden pointed out that it was "beyond question" that the parties intended "that the costs here sued for were not to be reimbursable" under the CPFF contracts, and that, accordingly, respondent's "recovery is a complete and unexpected windfall of $2,286,819.95" (R. 134). He was therefore of the opinion that recovery should have been denied on both claims (R. 135).

REASONS FOR GRANTING THE WRIT

The majority of the Court of Claims held that the determination that the costs were incurred incident to the performance of the CPFF contracts is a question of law (R. 121), and that therefore the decision of the Board of Contract Appeals in favor of the United States on the $980,000 claim was not entitled to the finality accorded by Article 16 to administrative resolution

of "disputes concerning questions of fact" and could be judicially reconsidered. At the same time it concluded that the decision of the first contracting officer against the United States on the identical question with respect to the 1¼ million dollar claim was binding and conclusive. In short, the Court of Claims has held that a contracting officer's decision adverse to the Government is binding but that one favorable to the Government may be reviewed and set aside. We believe that the obvious and far-reaching implications of such an inconsistent holding require its review by this Court. In addition, the Court of Claims avoided the binding effect of Article 16 with respect to the determination in favor of the United States by erroneously characterizing the factual issue involved as one of law. The net result of all this is to give respondent a windfall of 2¼ million dollars by awarding it reimbursement for expenses which, when the contracts were entered into, all parties concededly contemplated would not be reimbursable.

1. There is no doubt that the "Disputes" provisions in Article 16 of each of the CPFF contracts made final and conclusive only those administrative determinations concerning questions of fact (R. 80, Appendix, *infra,* p. 23). Consequently, if the Court of Claims was correct in holding that the question whether the developmental, engineering, and tooling costs were incurred incident to the performance of the CPFF

contracts was a question of law, we would agree that the parties and the court were not bound by the decision of the Board of Contract Appeals in favor of the United States on the $980,000 claim. It would also follow, if that holding was correct, that the first contracting officer's decision against the United States on the 1¼ million dollar claim would not be binding on the parties nor on the Court of Claims.

In holding that the 1¼ million dollar determination against the United States, although treated as a determination of law, was "conclusive and binding," the Court relied on Article 3 (b) of the contract (*infra*, p. 19). But Article 3 (b) simply authorizes the contracting officer to determine the amounts of reimbursable costs in accordance with certain Treasury Department regulations (R. 78, Appendix, *infra*, p. 19). Article 3 (b) has no express finalty clause nor any language from which a special finality provision should be implied.[4] The Court's holding that

[4] In holding that an Article 3 (b) determination of a question of law was binding and conclusive, the court below was apparently influenced by respondent's reliance in that court on *United States* v. *Moorman*, 338 U. S. 457. Article 15 in that case, like Article 16 here, limited finality to disputed questions of fact. The Supreme Court nevertheless held that the Contracting Officer's determination under Par. 2–16 (a) of the specifications was final and binding, whether the question was one of fact or law. But Par. 2–16 (a), unlike the Article 3 provisions here, stated "in language as plain as draftsmen could use that findings of the Secretary of War in disputes of the type here involved shall be 'final and binding.'" *United States* v. *Moorman*,

the first administrative determination against the United States on the 1¼ million dollar claim was final and binding is therefore in complete disregard of the contract provisions.[5] But at the very least, if Article 3 (b) is to be construed as a provision according finality to determinations of the contracting officer, it must make such determinations binding on both parties. By no proper process of reasoning can Article 3 (b) be read as making determinations against the Government conclusive, while leaving the Court of Claims free to reconsider identical determinations in the Government's favor.

2. The court's characterization of the administrative determinations here involved as legal,

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338 U. S. 457, 463. For the same reason, *United States* v. *Mason & Hanger Co.*, 260 U. S. 323, 325, is not in point here—the Article 4 in the contract in that case, unlike Article 3 here, expressly made the cost determination "final and binding."

Respondent also relied in the court below on *Great Lakes Dredge and Dock Co.* v. *United States*, 116 C. Cls. 679, 119 C. Cls. 504, now pending on petition for certiorari, No. 466, this Term. There, however, unlike the instant case, the Disputes Article did not limit finality to factual questions but expressly covered "all disputes concerning questions arising under this contract." 119 C. Cls. 504, 508.

[5] It is well settled that, absent any contractual provision according finality to administrative action, the Government may, as it did here, recoup moneys paid out by a public officer under mistake of either fact or law. *United States* v. *Wurts*, 303 U. S. 414; *Wisconsin Central R. R.* v. *United States*, 164 U. S. 190, 212; *United States* v. *Burchard*, 125 U. S. 176; *Heidt* v. *United States*, 56 F. 2d 559 (C. A. 5), certiorari denied, 287 U. S. 601; *United States* v. *Sutton Chemical Co.*, 11 F. 2d 24 (C. A. 4).

rather than factual, also constitutes, we submit, serious error warranting review here.

The "finality clause" in Article 16, which makes the administrative determination of all factual disputes final and conclusive, has been uniformly enforced by this Court in the several cases which have been brought here because of the continued "tendency in the Court of Claims to whittle away the authority of designated officers of the United States to make final decisions under contracts." See *United States* v. *Moorman,* 338 U. S. 457, 460, note 3; *United States* v. *Wunderlich,* 342 U. S. 98; *United States* v. *Callahan Walker Co.,* 317 U. S. 56. To the extent that the Court of Claims improperly characterizes factual questions as questions of law, the binding scope given Article 16 by this Court's decisions is largely nullified.

The administrative determination that the experimental, development, and tooling costs were not incurred incident to the performance of the CPFF contracts was solely one of fact. Despite the position taken by the Court of Claims, the construction of the terms of the contractual provisions authorizing reimbursement for certain costs was not in controversy. There was no dispute that experimental, development, and tooling costs previously incurred could in appropriate cases be reimbursed under CPFF contracts. The Board of Contract Appeals' decision proceeded on that assumption (R. 90). But whether

such costs were reimbursable in a particular case depended on whether they were "incident to and necessary for the performance" of the CPFF contracts in question (T. D. 5000, 26 C. F. R. 26.9 (a) Appendix, *infra*, p. 20).[8] The sole inquiry therefore in this case was whether and to what extent the costs had been incurred as a necessary incident of performance of the CPFF contracts. Such an inquiry, calling for examination of "all of the circumstances and facts involved" (R. 90) seems obviously a question of fact. Here, the circumstances and facts showed that when the CPFF contracts were negotiated, neither party intended to allocate the experimental, development, and tooling costs to the CPFF planes, that no such additional costs were included in the estimate of total CPFF costs, and that respondent fully amortized all of these costs against planes produced under the fixed-price contracts. The intent not to allocate any part of such costs to CPFF production, coupled with actual amortization of all of such costs against planes produced under the separate fixed-

[8] The Treasury Department Regulations contained in T. D. 5000 were promulgated pursuant to the Vinson-Trammel Act of March 27, 1934, as amended by the Acts of June 25, 1936, April 3, 1939, and June 28, 1940 (48 Stat. 505, 49 Stat. 1926, 53 Stat. 560, 54 Stat. 677; 50 U. S. C. App. 1153). These statutes limited profits on sales to the Government of Army and Navy vessels and aircraft. The regulations contained detailed provisions for determining reimbursability of costs incurred by contractors making such sales (Appendix, *infra*, pp. 20–22).

price contracts, could only mean that these costs were not incurred as a necessary incident of the CPFF contract performance. The contracting officer accordingly concluded that these costs "did not, in fact, represent costs of performing such CPFF contracts" (R. 89). Since the issue was factual, the decision of the Board of Contract Appeals affirming the contracting officer's decision on the $980,000 claim was final and binding and should not have been set aside by the court below. *United States* v. *Wunderlich*, 342 U. S. 98.[7]

3. Even if the question be treated as one of law which the Court of Claims was free to consider, we think its decision of that question was so clearly wrong as to warrant review by this Court. As Judge Madden pointed out, the decision gives respondent "a complete and unexpected windfall of $2,286,819.95" (R. 134) by allowing it to recover "for something [for] which, when it made the

[7] With respect to the 1¼ million dollar claim, we reserve the right, in the event the writ is granted, to contend that, treating the question as one of fact, the second contracting officer was free to reconsider his predecessor's determination—either on the ground that the decision of the first contracting officer was not a decision of a "dispute" within Article 16, or on the ground that, prior to final settlement of the contract, it was open to a contracting officer in any case to reconsider prior decisions of himself or his predecessor—and that the second contracting officer's decision upon such reconsideration, not having been appealed from (*United States* v. *Blair*, 321 U. S. 730, 734–736), is controlling and cannot be judicially reviewed.

contract under which it claims the payment, it intended that it should be paid nothing at all" (R. 133). The record is clear that at the time these CPFF contracts were entered into, all parties understood that no part of the experimental, development, and tooling costs previously incurred was to be a reimbursable item of cost. To allow respondent to recover in respect of those costs is to impose on the United States an obligation to which it never agreed.[8]

4. The questions are of general importance. We are informed by the Department of the Air Force that the provision embodied in Section 3 (b) of the instant CPFF contracts was a standard provision in CPFF contracts negotiated by

[8] The fact that respondent's decision to claim reimbursement for these expenses under its CPFF contracts was the result, at least in part, of pressure from the Bureau of Internal Revenue, with respect to taxes, does not justify the result reached by the Court of Claims. The Bureau had no power to amend the CPFF contracts or to determine what items should be reimbursable under them. Moreover, it is significant that the tax adjustment increased respondent's net tax liability by approximately $32,000, as compared with the amount of $2,286,819.25 here awarded respondent (R. 134). And, while the renegotiation agreement contemplated that the cost items here awarded respondent would be amortized against the CPFF contracts and not against the fixed-price contracts, respondent merely accepted a contingent liability in respect of them, agreeing to pay the United States $667,000 in the event that these expenses should be allowed and reimbursed under the CPFF contracts (R. 132). (The renegotiation agreement referred to covered profits for 1942. There were no deliveries under the fixed-price contracts after 1942 (R. 71, 76).)

the Air Force between 1940 and March 1949, numbering several thousand contracts involving hundreds of millions of dollars, and that since March 1949, a similar provision—differing principally in its reference to Part XV of The Armed Services Procurement Regulations, 32 C. F. R. (1950 Supp.) Part 414, rather than T. D. 5000 for the applicable cost principles—has been standard in CPFF contracts. It is of obvious importance in administering such contracts and in litigation arising under them to know whether the section will, despite the absence of any express language of finality, be construed as rendering final decisions of law of the contracting officer as to allowable items of cost. It is also of obvious importance in administering cost-plus contracts generally that the Government be not held liable for items of cost which the parties contemplated would not be reimbursable.

In addition, the decision below causes further confusion in the vexing area of finality of administrative decisions under Government contracts. In the first place, while we have repeatedly insisted that where a contractual provision calls for finality it be given effect, we think it no less important that where a contractual provision does not call for finality it should not be held to render decisions unreviewable. The holding that Section 3 (b), despite the absence of any language of finality, rendered conclusive against

the Government the first contracting officer's decision plainly violates this principle. In the second place, the decision below, if unreviewed, affords an opportunity for undercutting the standard "disputes" provisions, contained in Section 16 of these contracts, by erroneously characterizing as questions of law issues which are really questions of fact. Finally, the decision indicates the tendency of the Court of Claims to apply the rule of finality unequally. Given two administrative determinations of the identical issue, that court reaches the extraordinary result that the one adverse to the Government is final and cannot be reconsidered, while that favorable to the Government can be reconsidered. It does this by misconstruing Section 3 (b) in the one case and ignoring it in the other and by erroneously characterizing issues of fact as issues of law. The implications of such a holding clearly call for review by this Court.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be granted.

PHILIP B. PERLMAN,
Solicitor General.

JANUARY 1952.

APPENDIX

1. Each of the four CPFF contracts contains the following provisions (R. 77–78):

ARTICLE 3. CONSIDERATION

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the Contract, subject to reimbursement for cost, as outlined in Article 6 hereof, the cost, plus a fixed fee of * * * being * * * percent of the total estimated cost of * * *. This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

(b) For the purpose of determining the amount payable under this Contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

(1) All costs which have been incurred by the Contractor in anticipation of this Contract and prior to the signing thereof, and which if incurred after the signing of this Contract, would have been considered as allowable items of cost within the meaning of said Regulations, shall be considered as allowable items of cost incurred hereunder.

2. The Treasury Department regulations referred to in Article 3 (b) of the contracts *supra*, provide in pertinent part (26 C. F. R. 26.9, 1940 Supp.):

> § 26.9 *Cost of performing a contract or subcontract*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract; and (2) the proper proportion of any indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.
>
> (b) *Elements of cost.*—No definitions of the elements of cost may be stated which are of invariable application to all contractors and subcontractors. In general, the elements of cost may be defined for purposes of the Act as follows:
>
> (1) Manufacturing cost, which is the sum of factory cost (see paragraph (c) of this section) and other manufacturing cost (see paragraph (d) of this section);
>
> * * * * *

(c) *Factory Cost.* Factory cost is the sum of the following:

* * * * *

(5) *Indirect factory expenses.* Items, usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

* * * * *

(iv) *Fixed charges and obsolescence.* Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable standby equipment; and depreciation and obsolescence of special equipment and facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the Department concerned has made a certification binding upon the Commissioner of Internal Revenue, pursuant to section 4 of the Act, in the case of such contract or subcontract. * * *

* * * * *

(d) *Other manufacturing cost.* Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs which are not properly or

satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

* * * * *

3. a. The Disputes Article in three of the CPFF contracts provides (R. 80):

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

b. The Disputes Article in the fourth CPFF contract provides (R. 81):

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. * * * Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance

of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

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NO. 13

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BRIEF FOR THE RESPONDENT IN OPPOSITION

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CITATIONS

STATUTE:

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T.D. 5000, 26 C.F.R. (1940 Supp.) 4, 9, 13

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ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINION BELOW

The opinion of the Court of Claims (R. 101) is not yet reported.

JURISDICTION

The judgment of the Court of Claims was entered on October 2, 1951 (R. 135). Upon timely application, the time for filing petition for certiorari was extended to January 30, 1952 (R. 136). The jurisdiction of this Court is sought to be invoked under U.S.C. Title 28, Section 1255 (1).

QUESTIONS PRESENTED

The Court below gave respondent judgment for those portions of certain capitalized experimental, development and production tooling costs which respondent charged to four cost-plus-fixed-fee contracts with petitioner for the manufacture of P-39 military airplanes. Proper portions of such deferred costs were clearly reimbursable under the terms of the contracts. No specific consideration was given the question of reimbursement of these costs in the negotiation of the contracts, and, at the time, respondent did not intend to seek reimbursement. Part of the costs were allowed by one Contracting Officer and paid. The remainder was disallowed by a successor Contracting Officer. The amount paid was recouped by action of the General Accounting Office. The decision of the second Contracting Officer was appealed to the War Department Board of Contract Appeals, which made its own findings of fact and disallowed the vouchers before it. The fact findings of the Court of Claims were in all respects the same as those of the Board of Contract Appeals. The questions presented are:

1. Did the Court of Claims correctly rule that since the contract terms clearly made these costs reimbursable and no specific consideration was given to the question of the reimbursement in the negotiation of the contracts, respondent could recover notwithstanding the fact that the accounting method respondent was using at the time three of the CPFF contracts were entered into evidenced a lack of intent to seek reimbursement?

2. Did the Court of Claims correctly rule that since the Board of Contract Appeals and the Court of Claims made the same findings of fact, the only issue was one of law as to which the disputes clause of the contracts

did not give finality to the decision of the Board of Contract Appeals?

Petitioner claims that the case presents questions (a) as to the finality of the decision of the first Contracting Officer and (b) as to the Court of Claims inconsistency in giving it finality while holding reviewable the decision of the Board of Contract Appeals affirming the second Contracting Officer. This case does not present these questions because the Court of Claims actually reviewed the decision of the first Contracting Officer on its merits and sustained it.

CONTRACT AND REGULATION PROVISIONS INVOKED

Pertinent portions of the contract and provisions of the regulations are set forth in the Appendix to the Petition at pages 19 through 24.

STATEMENT OF THE CASE

Respondent sued on four cost-plus-fixed-fee contracts, hereinafter referred to as CPFF contracts, with the United States for the manufacture and delivery of military aircraft known as P-39's. The scheme of each of these contracts was that the contractor would be reimbursed for his manufacuring costs and would, in addition, receive a fixed fee for performing the contract (R. 77). The amount of the fee was arrived at by negotiations between the parties and cost estimates submitted by the contractor were considered in the negotiations (R. 91, 126). However, there were no negotiations between the parties about the contract terms relating to cost reimbursement. Each contract provided that (R. 78):

> "... allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated by the Treasury Depart-

ment in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T.D. 5000 and approved by the Secretary of War August 2, 1940."

TD 5000 (R. 78-80) was promulgated under the so-called Vinson Act, as amended by the Act of June 28, 1940 (54 Stat. 676), and was approved by the Secretaries of the Navy and the Treasury, as well as the Secretary of War.

The first Contracting Officer who passed on the questions whether certain experimental, development and production tooling costs were properly payable to respondent under the terms of TD 5000 decided that the costs were reimbursable and approved the vouchers which were before him (R. 85). The record shows that some of this Contracting Officer's subordinates recommended against the allowance of the vouchers and that others recommended that they be allowed (R. 85). While the approval of the vouchers did not require any express findings of fact, the fact that they were approved clearly means that to the extent the Contracting Officer decided fact issues he decided them in favor of respondent and that to the extent he decided legal issues he likewise decided these in favor of respondent. Plaintiff was paid $1,299,856.02, the amount allowed by the first Contracting Officer (R. 85). This amount was subsequently recouped by action of the General Accounting Office from other money due from petitioner to respondent (R. 87-88).

Another series of vouchers for $986,963.93 was submitted to a successor Contracting Officer, who held that respondent was not entitled to reimbursement (R. 86). These vouchers were for additional amounts of the deferred costs and the question of their reimbursability

was exactly the same as the question of reimbursability of the vouchers approved by the first Contracting Officer. The second Contracting Officer's decision was appealed to the War Department Board of Contract Appeals (hereinafter called the Board) which made its own findings of fact (R. 91), but arrived at the same conclusion (R. 92). It did not approve or endorse the second Contracting Officer's findings of fact.*

The Court of Claims found that the second Contracting Officer did not act upon the vouchers which had been approved by the first Contracting Officer (R. 115). The Board, in connection with the appeal from the ruling on vouchers presented to the second Contracting Officer, noted that "the parties considered the appeal to include only" the vouchers for $986,963.93, and consequently limited its decision to those (Tr. Stip. Ex. P, p. 10). Under these circumstances, petitioner's statement (Pet. 8-9) that "Respondent took no appeal from the [second] Contracting Officer's denial of the 1¼ million dollar claim. . . . " is misleading, for there was no occasion for such an appeal.

After the decision of the Board this suit was begun to recover the amount recouped by the General Accounting Office plus the amount disallowed by the Board. The Court of Claims gave respondent a judgment for both amounts (R. 101).

In the absence of a showing of fraud on the part of the Board, its fact findings are final and binding on respondent.

Respondent did not challenge the facts found by the Board. Respondent's position, which was sustained by

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* Petitioner, ignoring this fact, recites (Pet. 8) findings of fact made by the second Contracting Officer, which are obviously irrelevant in the light of the findings on appeal made by the Board of Contract Appeals.

the Court, was that the facts found by the Board clearly justified reimbursement of the costs. The Board findings upon which respondent relied were the following (R. 90):

> "There is no dispute between the parties as to the amount of the costs or as to the propriety of the method of allocation used by appellant. . . .
>
> "The experimental and development costs are clearly within the category of indirect costs as defined by T.D. 5000 and are specifically covered by Section 26.9(d) of T.D. 5000—set out above. . . . Section 26.9(e)(5)(D) of T.D. 5000 set out above also provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. It is clear from the record and evidence that the production tooling was used in the performance of CPFF contracts calling for the production of the P-39 type of airplane. It would seem, therefore, that items of this type are within the intent and meaning of T.D. 5000."

The experimental and development costs were incurred by respondent between 1936 and 1939 in connection with the manufacture of experimental airplanes. Since the experiments had resulted in new aeronautical designs and principles of value to respondent, their cost to respondent was capitalized in order that it might be charged off against production contracts for airplanes incorporating the new designs and principles. As the Board found, *supra*, the P-39's manufactured under the CPFF contracts incorporated these designs and principles.

Beginning in 1939 respondent entered into a series of fixed-price contracts for P-39's with both the British Government and the United States (R. 70). To

perform these contracts, and in anticipation of others, respondent acquired a large amount of production tooling usable only for the manufacture of P-39's (R. 72). The cost of this tooling was capitalized in order that it might be charged off against production contracts on which the tooling was used (R. 73). As the Board found, the tooling was used in the manufacture of P-39's under the CPFF contracts.

The findings of fact of the Board and the Court of Claims were the same on every point. The administrative decision and the Court's decision differed only in the result. The difference depended wholly upon the legal significance of certain undisputed facts which are, respondent believes, unique.

When production under the fixed-price contracts started in 1940 the respondent began to charge off the experimental, development and tooling costs it had capitalized (R. 76). Beginning in 1941 respondent began to enter into CPFF contracts for P-39's (R. 76). However, despite the fact that the CPFF contracts were for the manufacture of the same airplanes as were being manufactured under the fixed-price contracts, respondent, on its books, treated all the experimental, development and tooling costs as costs of the fixed-price contracts (R. 74). Upon an audit of respondent's tax returns, however, the Bureau of Internal Revenue took the position that, since the new aeronautical principles and designs were incorporated in all P-39's, and since the tools were being used to manufacture P-39's under the CPFF contracts, the whole amount of the deferred experimental, development and tooling costs was not a cost of performing the fixed-price contracts but was, in part, a cost of performing the CPFF contracts (R. 81). The Bureau insisted that respondent revise its books to reflect the true

facts. Since the Bureau's position was unquestionably correct respondent, after an initial period of remonstrance on other grounds, restored the proper amount of the costs to its books (R. 84). Respondent then requested reimbursement for the costs so restored under the terms of the CPFF contracts (R. 85).

As has been pointed out, part of the restored costs was allowed by the first Contracting Officer, paid to respondent and later recouped by petitioner. The remainder was disallowed by the Board principally because no portion of these costs was included in the cost estimates respondent submitted for the purpose of negotiating the fixed fees under the CPFF contracts, and because respondent's accounting at the time the CPFF contracts were entered into did not contemplate reimbursement for the costs. The Board concluded from the latter fact that *respondent* had no intention of seeking reimbursement of the costs at the time the contracts were negotiated (R. 91).

Petitioner's treatment of this point is less than candid. At six places in the petition, beginning with the Questions Presented, petitioner states in substance that at the time the contracts were made *both* parties contemplated that the costs would not be reimbursable. (Pet. 2, 4, 10, 14, 16, 17). At no place does petitioner advise the Court that this is *petitioner's fact contention* based upon the portion of the dissenting opinion of Judge Madden quoted at page 9 of the petition and *not supported by the facts found by the Board and the majority of the Court of Claims.* On this point the Board said (R. 91):

> "It is clear from the record that no portion of these costs was included in the estimates under the CPFF contracts and *no specific consideration was given to the question of reimbursement in the*

negotiation of the subject contracts." (Emphasis added)

The Board and the majority of the Court found that respondent's conduct during the negotiation of the CPFF contracts indicated that *respondent* had no intention of claiming reimbursement for the costs at that time.* Neither of them found that *both* parties had this intention and they both found that the contract terms clearly provided for reimbursement (R. 91, 126-129). Petitioner skips from the fact that respondent did not intend to claim reimbursement for certain costs to the conclusion that both parties intended that such costs should not be reimbursable under the contract.

That, as the Board found, the reimbursement of these particular costs was never specifically considered in connection with the negotiation of these particular contracts is crystal clear from the fact that all contracts incorporated, without the change of a single term, the provisions of Section 26.9 of TD 5000, a Treasury regulation promulgated long before the first of these contracts was signed.

The Court below concluded that respondent's intention was not a pertinent fact which kept it from recovering in the circumstances of this case (R. 128).

There was no question of unconscionable profit on the part of the respondent. The contracts were subject to renegotiation and part of respondent's recovery in this case must be paid to the petitioner under an existing renegotiation agreement (R. 132). In addi-

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* Both the Board and the Court were partially wrong in this conclusion because the Contracting Officer entered into the fourth and final CPFF contract with respondent shortly *after* he had approved for reimbursement the first vouchers respondent submitted claiming the experimental, development and tooling costs (R. 77, 84-86).

tion, since all the costs involved here were actually allowed for tax purposes, although spread over all the years during which respondent performed both the fixed-price and CPFF contracts, the entire amount of respondent's recovery will add to its net income and thus be taxable.

REASONS FOR DENYING THE WRIT

There are three reasons for denying the writ:

I. No important issue of Federal law is involved. The case raises only one ordinary question of contract law which depends entirely upon the facts of this particular case, and which was correctly decided by the Court of Claims.

II. The case does not involve a construction of the standard disputes clause. The Board of Contract Appeals decided certain legal questions on the basis of findings of fact which respondent did not dispute. On the same facts the Court of Claims reached contrary conclusions of law. The disputes clause makes the administrative decision binding as to facts only.

III. The case does not raise a question as to the finality of a Contracting Officer's allowance of costs under contractual provisions similar to Section 3 of the contracts sued on for the reason that here both the first Contracting Officer's determination and the decision of the Board of Contract Appeals were reviewed both as to the facts and the law by the Court of Claims. The determination of the first Contracting Officer was affirmed on both the facts and the law; the facts found by the Board of Contract Appeals were approved but its decision on the law was reversed. Furthermore, the

Court of Claims considered the finality of the Contracting Officer's allowance only in connection with petitioner's claim that respondent had not exhausted its administrative remedies.

I

THE CASE RAISES ONLY AN ORDINARY QUESTION OF CONTRACT LAW DEPENDING ENTIRELY ON THE PARTICULAR FACTS INVOLVED. THE ISSUE WAS DECIDED CORRECTLY.

The only substantial question in this case was whether recovery was precluded by the fact that at the time the CPFF contracts were negotiated respondent did not intend to claim reimbursement for the experimental, development and production tooling costs.* The legal effect of this intention, in the light of the other circumstances of the case, including the fact that a contrary intention was clearly expressed by the contracts, raised only an ordinary question of contract law. The Court of Claims, while agreeing with the Board as to the fact of respondent's intention, found that it was not a "condition" or "pertinent fact" which made the costs non-reimbursable under the CPFF contracts (R. 128). The Court pointed out that the respondent was under no contractual obligation to request reimbursement for any particular cost, but that the contracts did obligate the Government to reimburse respondent for any cost made reimbursable by the contracts if, as here, reimbursement was requested (R. 128).

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* Although the Board of Contract Appeals relied principally on this intention in denying respondent relief, it made a number of subsidiary fact findings upon which it also relied. None of these fact findings were in dispute. The Court of Claims dealt with each of them separately and held each of them without legal significance in this case. Petitioner does not mention any of these subsidiary issues and apparently does not rely on them.

That this holding was right is clear from the following material and decisive facts, all of which appear either in the contracts themselves or in the opinion of the Board of Contract Appeals (R. 90), and some in both places:

(a) The parties did not give any specific consideration to the costs sued for while the contracts were being negotiated (R. 91).

(b) The terms of the contracts which defined what were allowable costs were written by the petitioner long before these contracts were entered into and were not decided upon as a result of negotiations for these particular contracts (R. 78).

(c) The contract terms were not ambiguous and clearly made such costs reimbursable, thus expressing an intention contrary to that evidenced by respondent's accounting practices at the time the contracts were signed (R. 90, 125).

(d) The production tooling was used in the manufacture of P-39's and thus a proper portion of the costs of the tooling was a cost of manufacturing P-39's under the CPFF contracts (R. 124, 130).

(e) P-39's manufactured under the CPFF contracts incorporated the aeronautical designs and principles resulting from respondent's experimental and development work, and thus a proper portion of the cost of those designs and principles was a cost of manufacture under the CPFF contracts (R. 123, 130).

We submit that the question of which of the undisputed facts peculiar to this case are legally material is simply a question of ordinary contract law, and that no question of general interest or importance is raised. We also submit that the Court of Claims correctly ruled that the case was governed by the fact that the costs

sued for were actual costs of manufacturing the P-39's under the CPFF contracts and that the contract terms clearly made them reimbursable.

II

THE FACTS FOUND BY THE COURT OF CLAIMS WERE THE SAME AS THOSE FOUND BY THE BOARD OF CONTRACT APPEALS AND THE DISPUTES CLAUSE OF THE CONTRACTS DID NOT MAKE THE DECISION OF THE BOARD ON LEGAL QUESTIONS BINDING ON THE COURT OF CLAIMS.

The question of which of the facts found by the Board of Contract Appeals were controlling was clearly a question of law as to which respondent was not bound by the decision of the Board of Contract Appeals under the disputes clauses of the contracts which made the Board's determination final and conclusive on "all disputes concerning questions of fact" (R. 80, 81).

Petitioner says that "The sole inquiry therefore in this case was whether and to what extent the costs had been *incurred* as a necessary incident of performance of the CPFF contracts", and that such an inquiry is "obviously a question of fact" (Pet. 14, emphasis added). This is a complete misstatement of the issue. The terms of TD 5000 clearly make current charges for capital assets used in the performance of the contracts reimbursable, no matter when the cost of such capital assets was incurred, or for what reason (R. 79). There is no question about the proper portion of these particular capital assets being an actual cost of performing the CPFF contracts. The first Contracting Officer, the Board of Contract Appeals and the Court of Claims all held that they were. The Board of Contract Appeals held that nevertheless certain other undisputed facts precluded respondent from recovering. The Court of Claims simply held that they did not.

That the Board was deciding a question of law is clear from its own opinion (R. 90, 118-119).

III

A RULING BY THIS COURT THAT THE DECISION OF THE FIRST CONTRACTING OFFICER WAS NOT FINAL AND BINDING ON PETITIONER WOULD NOT CHANGE THE RESULT.

Petitioner states that the Court of Claims held that the decision of the first Contracting Officer under Section 3 of the contract was final and binding on the Government (Pet. 10); that Section 3, in substance, is used widely in Government contracts (Pet. 16); and that this question is one of wide general interest.

Actually, the decision of the first Contracting Officer allowing vouchers for one and one-quarter million dollars of the costs sued for was reviewed on its merits both as to facts and law by the Court of Claims, and affirmed. Therefore, the case does not actually raise a question of whether the decision of the first Contracting Officer was binding on petitioner. Regardless of whether the Court had held the decision of the first Contracting Officer final and binding on the Government, or, on the contrary, fully reviewable, the Court's conclusion would have been precisely the same.

That the issue which petitioner seeks to raise is in fact moot is, in itself, an adequate answer to the petition in this respect. It may be well, however, since petitioner has not seen fit to do so, to explain briefly how the matter of the effect of the decision of the first Contracting Officer arose in the Court of Claims' opinion. The whole of this discussion was under the heading "Alleged failure of plaintiff [respondent] to exhaust its administrative remedies" (R. 109). *Petitioner* contended that the one and one-quarter million dollar claim was not before the

Court of Claims because the first Contracting Officer had been overruled by the second Contracting Officer and respondent had not appealed from *that* portion of the second Contracting Officer's decision (R. 113). The Court of Claims discussed the effect of the first Contracting Officer's decision *only* in connection with the contention of the petitioner that respondent had failed to exhaust its administrative remedies (R. 109-116).

In disposing of this contention, the Court of Claims held that the decision of the second Contracting Officer dealt only with the vouchers before him for action, that he did not reverse the decision of the first Contracting Officer (R. 115-116) and that, therefore, the respondent's suit in the Court of Claims for the amount of the approved vouchers was not barred.*

After discussing petitioner's administrative defenses, the Court said (R. 121):

> "We now turn to the parties' position concerning the merits of the controversy on the law and on the facts."

The Court then proceeded to discuss the merits of the whole case without regard to whether they were involved in the decision of the first Contracting Officer or of the Board.

Dissenting Judge Madden agreed that respondent's claim was not barred by failure to exhaust administrative remedies (R. 134), and the Court was unanimous on this point. Judge Madden did take the position that the Government would not be bound by a mistake of law on the part of the first Contracting Officer and that, therefore, questions of law decided by the first Contracting Officer were open for review by the Court of

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* The amount of these vouchers was paid and then recouped from other amounts owing from petitioner to respondent.

Claims (R. 135). The fact is, however, that the Court of Claims did review all questions of law which could have been decided by the first Contracting Officer, and resolved them all in favor of respondent (R. 121-132).

Just what the Court of Claims actually determined as to the effect of the decision of the first Contracting Officer, in the context of this procedural argument by petitioner as to the exhaustion of administrative remedies by respondent, is not wholly clear. Its remarks on the "conclusiveness of the decision" (R. 113, 116) are fully consistent with its conclusion that upon both the facts and the law the first Contracting Officer was correct. The review by the Court of Claims of the decision of the first Contracting Officer was not in any way confined to questions of fraud, good faith or honest judgment. The Court not only reviewed all the questions of law which could have been involved in the first Contracting Officer's decision but, in view of petitioner's attempt to overcome fact findings of the Board which were favorable to respondent, the Court also took evidence on and made findings about every fact in the case (R. 67-100). Its fact conclusions were the same as the Board's.

The consideration of petitioner's argument, however, shows that petitioner itself is guilty of urging the same kind of inconsistency with which it charges the Court of Claims on pages 9 and 10 of the Petition. There it charges that the Court held that the decision of the Board of Contract Appeals was not a dispute concerning questions of fact and could be judicially reconsidered and, at the same time, concluded that the decision of the first Contracting Officer against the United States on the identical question was binding and conclusive. As we have already demonstrated, this difference is only apparent, not real, for the reason that the Court of Claims actually reviewed the decision of the

first Contracting Officer on its merits. The position petitioner wishes this Court to take, however, is that the decision of the first Contracting Officer involved questions of law and was fully reviewable by the Court (Pet. 11), whereas the decision of the Board on the same issues involved questions of fact and was, therefore, final and binding on respondent under the disputes clause (Pet. 15).

CONCLUSION

For all these reasons we respectfully request that the petition for the writ be denied.

Respectfully submitted,

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March, 1952

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In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 13

THE UNITED STATES, PETITIONER

v.

BELL AIRCRAFT CORPORATION

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the Court of Claims (R. 101-135) is reported at 120 C. Cls. 398.

JURISDICTION

The judgment of the Court of Claims was entered on October 2, 1951 (R. 135). On December 29, 1951, the Chief Justice extended the time for filing a petition for certiorari to and including January 30, 1952 (R. 136). The petition, filed on that date, was granted on March 31, 1952 (R. 139). The jurisdiction of this Court rests upon 28 U.S.C. 1255(1).

QUESTIONS PRESENTED

Respondent claimed approximately 1¼ million dollars and, later, an additional and separate

amount of $980,000, for reimbursement of certain costs under its cost-plus-a-fixed-fee contracts with the United States.

The questions presented are:

1. Whether the determination that the claimed costs were not incurred incident to and necessary for the performance of the cost-plus-a-fixed-fee contracts was a determination of fact within the standard form contract provision that administrative decisions "on all disputes concerning questions of fact * * * shall be final and conclusive upon the parties * * *."

2. Whether the Court of Claims may set aside such an administrative determination in favor of the Government as to the $980,000 claim and substitute its own judgment for that of the administrative agency.

3. Whether a similar determination with respect to the 1¼ million dollar claim, made after that claim had been initially allowed but later recouped, is final and binding in the absence of an appeal to the department head or his representative in accordance with the standard provisions of the contracts.

4. Whether the provision in the contracts stating that "allowable items of cost will be determined by the contracting officer" and containing no language giving his determination finality makes the initial allowance of the 1¼ million dollar claim final and

prevents a successor contracting officer from recouping and disallowing that claim.

5. Whether, under the foregoing provision, the Court of Claims had any warrant in holding conclusive the initial allowance of the 1¼ million dollar claim in favor of the contractor, while denying conclusiveness to the successor contracting officer's disallowance of the $980,000 claim in favor of the Government.

6. Whether, assuming the question was properly before it for decision, the Court of Claims erred in awarding reimbursement, under cost-plus-a-fixed-fee contracts, for items which the parties understood, when the contracts were entered into, would not be claimed as reimbursable costs.

CONTRACT AND REGULATION PROVISIONS INVOLVED

The pertinent portions of the contract and regulation provisions are set forth in the Appendix, infra, pp. 51-56.

STATEMENT

This action arises out of respondent's claims for reimbursement of certain costs under its cost-plus-fixed-fee (CPFF) contracts with the United States. The costs in question comprise about two-thirds of certain experimental, developmental and tooling expenses incurred by respondent some time prior to the entry into the CPFF contracts here in question. The issue which became the subject of a dispute between the United States and respondent was whether respondent, having initially charged

off those expenses in their entirety against certain fixed-price contracts not here involved, could reallocate those expenses between the two groups of contracts so as to recover a proportionate part of them as costs of the CPFF contracts which are in issue in the present case. An Army contracting officer and Board of Contract Appeals resolved that issue against respondent, refusing to allow any part of the claimed costs against the CPFF contracts. The Court of Claims allowed respondent the entire costs claimed by it, aggregating $2,286,819.95.

In 1936-1938, respondent, in four separate contracts, agreed to build 16 experimental or test fighter planes for the United States (R. 67). Three contracts called for delivery of 15 fighter planes to the Army Air Corps at a total fixed-price of $3,804,445. (R. 67). The fourth contract, also negotiated on a fixed price rather than CPFF basis, required delivery of the sixteenth plane to the Navy at a cost of $245,000 (R. 67). The total contract price thus paid to respondent for these 16 fighter planes aggregated $4,049,445, or an average of over $253,000 per plane (R. 67). However, in performing these four fixed-price contracts, respondent "incurred substantial expenditures over and above" the total contract price (R. 67). These excess expenditures, amounting to an additional $1,528,760.66, were labeled by respondent as "experimental and development costs" and set up on its books as deferred charges applicable to anticipated future produc-

tion (R. 35, 37, 38). Respondent deferred and capitalized these charges as follows (R. 69):

December 31, 1938	$ 128,052.77
December 31, 1939	511,776.21
December 31, 1940	888,931.68
	$1,528,760.66 [1]

On April 26, 1939, respondent entered into another contract with the Air Corps for the delivery of 14 additional service test models of the P-39 fighter plane at a fixed price of $1,073,445, or about $76,500 per plane (R. 70, 71). Thereafter, in 1939-1941, respondent was awarded several fixed-price production contracts by the Air Corps calling for the delivery of 952 P-39 fighter planes at a cost of about 36½ million dollars, or approximately $38,000 per plane (R. 71). During this same period, respondent also received additional fixed-price contracts from the British Government for the production of 810 P-39's for almost 34 million dollars (R. 71).

The mass production of this large quantity of planes for the United States and Great Britain required respondent to incur production tooling costs in 1939 and 1940 amounting to $1,894,109.57.[2]

[1] This was later adjusted to $1,499,739.23 after audit by the Army Audit Agency (R. 70).

[2] This was later adjusted to $1,874,725.77 after audit by the Army Audit Agency (R. 72). Production tooling differs from ordinary machine tools in that the latter, which consist of lathes and drill presses, can be adapted to many uses and are not restricted in use to the specific model or type of

In December, 1940, respondent added this sum to the deferred charges it had set up for the excess experimental and development costs and re-designated the account as "Experimental, Development and Production Tooling Expenses" (R. 72). By the end of 1942, respondent had fully amortized the entire amount of this account by charging all of the deferred production tooling costs and all of the deferred experimental and development costs in the account against deliveries of the P-39 planes in 1940 through 1942 under its fixed-price contracts with the United States and Great Britain (R. 76). Even after all of these deferred costs, which totalled over 3 million dollars, were so charged to the cost of the airplanes sold under the fixed-price contracts, respondent realized a net profit on these fixed-price contracts, before taxes and renegotiation of excess profits, of $18,280,732.50, or a profit of about 25 percent of the total value of $71,364,004.86 for these fixed-price contracts (R. 64, 71, 98).

In the meantime, between August 14, 1941, and April 13, 1945, respondent was awarded a series of CPFF contracts by the Air Corps for the production of over 10,000 additional P-39 planes at a total estimated cost of 307 million dollars plus a fixed fee of over 14 million dollars (R. 76-77). Three of the four contracts, calling for the production of over 5,000 planes, were entered into in 1941

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product manufactured (R. 72). The production tooling for the P-39 plane was largely assembly line fixtures, and special blocks and dies which remained in use only as long as the P-39's were in production (R. 72).

and 1942, while respondent was still amortizing its experimental, development and tooling costs solely against the fixed-price contracts (R. 77). A fourth contract, and a substantial increase in one of the others, were entered into after those expenses had been completely amortized (R. 77).

In the course of the negotiations for the CPFF contracts it was understood by both parties that respondent did not intend to allocate any of the deferred costs against production under the CPFF contracts and therefore did not include any part of such costs in its cost estimates for those contracts (R. 76, 82, 125). Respondent's "Annual Report for 1940" described these deferred costs which amounted to over 3 million dollars "at December 31, 1940" and stated that the "Company is at present concentrating on the manufacture of Airacobras [P-39's], and it is the Company's intention to absorb the aggregate of the foregoing charges on the basis of the quantities of this model under contract" (R. 76). Respondent's "Annual Report for 1941", prepared after at least two of the CPFF contracts had been negotiated, reiterated that the "Experimental, Development and Production Tooling Expense" account of $3,352,096.78 had been deferred "at December 31, 1940, to be absorbed on the basis of certain quantities of aircraft under contract." (R. 76). No planes were under CPFF contract as of December 31, 1940 (R. 77). The only aircraft under contract as of December 31, 1940 were those called for under

the fixed-price contracts with the Air Corps and the British Government (R. 71).

In March, 1942, the Bureau of Internal Revenue audited respondent's income tax returns for 1941 and prior years and requested that respondent, "for income tax purposes," allocate the deferred experimental, development and tooling costs to all P-39 production under both the CPFF contracts and the fixed-price contracts (R. 49, 81). Respondent refused to comply and, as already noted, continued to amortize the deferred costs solely against the fixed-price contracts until the end of 1942, when all the costs were fully charged off to the fixed-price contracts (R. 76, 81-82). In September, 1942, respondent explained this refusal to comply with the Bureau's request by stating that (R. 82):

> This item [deferred experimental, development and production tooling costs] should be allowed as an amortization expense against the fixed price contracts only in view of the fact that *any amortization to be allowable under a cost-plus-fixed-fee contract would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost plus contracts* in view of the position taken by the Government that prior to our entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses. [Italics supplied.]

The Bureau, however, adjusted respondent's income for 1941 and 1942 by allocating the deferred

charges to future P-39 production under the CPFF contracts as well as the P-39's delivered in 1941 and 1942 under the fixed-price contracts. This adjustment increased respondent's income for 1941 and 1942 and therefore increased its tax liability for those two years by $1,337,474.89. (R. 60). The same adjustment allowed deduction of a portion of the deferred charges against deliveries under CPFF contracts in 1943, 1944 and 1945 and therefore decreased respondent's taxes for those three years by $1,305,418.72. (R. 94). Thus, respondent's net tax liability was increased by only $32,056.17 as a result of the Bureau's reallocation of the deferred charges. (R. 60, 134).

In April, 1943, respondent's comptroller submitted to the Air Corps a statement of accounting policies pertinent to the company's operations under the CPFF contracts, reiterating that the deferred costs were chargeable only to fixed-price production (R. 82):

> Experimental, development and production tooling expenses are written off against the deliveries of the items to which expenditures apply. No experimental expense is charged to overhead applicable to CPFF contracts.

Six months later, respondent wrote to the Price Adjustment Office in charge of renegotiating respondent's excessive profits for 1942, proposing to reallocate its deferred charges as required by the Bureau of Internal Revenue "provided that the amounts disallowed by you against fixed price con-

tracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office" (R. 83). The proposed reallocation would have increased respondent's excessive profits for 1942 by $667,000 and would have made respondent liable to refund that additional amount to the United States (R. 94).[3] The renegotiation agreement entered into between respondent and the United States for 1942 did not, however, compute respondent's excessive profits on the basis of the proposed reallocation. Instead, it allowed respondent to charge all of the deferred costs to the P-39's produced under the fixed-price contracts (R. 93-94). The agreement further provided that the proposed reallocation of deferred costs to CPFF contracts and fixed-price contracts "has been tentatively approved by the Army Air Forces," and (R. 94)

> * * * if the amount allocated to the CPFF Contracts is finally approved by both the Army Air Forces and the General Accounting Office of the Comptroller General of the United States, and reimbursement therefor, is made, the Contractor agrees to pay to the United States as an additional refund the sum of $667,000, on account of which the Contractor shall receive credit for Federal Income and Excess Profits Taxes thereon as determined by the Bureau of Internal Revenue * * *.

[3] Of course, the proposed reallocation was conditioned on respondent's being reimbursed under the CPFF contracts for the amount claimed in this suit, $2,286,819.95.

Shortly after the tentative approval of the proposed reallocation for renegotiation purposes, respondent, on September 9, 1943, restored to the deferred account, which it had already fully amortized against the fixed-price contracts, a proportion of the experimental, development and tooling expenses which it considered applicable to the CPFF contracts in accordance with the new plan of amortization (R. 84). The sum so restored amounted to $2,286,819.95, the unrestored difference of $1,087,645.05 remaining applicable to the fixed-price contracts (R. 84-85).

Claiming that it was entitled to reimbursement under the CPFF contracts for the $2,286,819.95 in experimental, development and tooling expenses [4] allocated by it on its books to CPFF production, respondent submitted two sets of vouchers to the Air Corps for payment of that sum (R. 85). The first set of vouchers, allocated to deliveries under the CPFF contracts from 1942 to August 1943, and submitted in September, 1943, amounted to $1,299,856.02 (referred to as the 1¼ million dollar claim) (R. 52, 85). The second set of vouchers, allocated

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[4] Respondent was reimbursed by the United States under the CPFF contracts for production tooling costs incurred after performance of the CPFF contracts had begun. Respondent's Chief Accountant testified that "tooling which was produced during the life of the CPFF contracts and which was built in connection with CPFF contracts was paid for under the CPFF contract" (Transcript, p. 268). The production tooling costs claimed here as being reimbursable under the CPFF contracts are the costs incurred in 1939 and 1940 in connection with the mass production of P-39's under the fixed-price contracts and before any of the CPFF contracts had been awarded. See *supra*, p. 5; (R. 99).

to deliveries under the CPFF contracts after August 1943, and submitted in October 1943, amounted to $986,963.93 (referred to as the $980,000 claim) (R. 85).

The Assistant Resident Auditor for the Air Corps recommended that the vouchers for the 1¼ million dollar claim be rejected because: (1) all of the deferred costs have been charged off to the fixed-price contracts "in the period prior to the inception of [the] CPFF contracts", and (2) the deferred costs were losses suffered by respondent in performing the fixed-price experimental contracts in 1936-1938 and there was no provision in the CPFF contracts for reimbursement of such losses (R. 85). This recommendation was rejected by the Resident Auditor for the Air Corps, who certified the vouchers to the Contracting Officer by whom they were approved for reimbursement under the CPFF contracts (R. 85). The 1¼ million dollar claim was accordingly paid to respondent by the United States, but later recouped after objection by the Comptroller General (R. 85, 87).

The same Assistant Resident Auditor recommended rejection of the October, 1943 vouchers for the $980,000 claim for the same reasons he had urged against the earlier claim (R. 86). By this time, the former Resident Auditor and the former Contracting Officer had been replaced (R. 86). Their successors accepted the Assistant Resident Auditor's recommendation and declined to approve the vouchers for the $980,000 claim (R. 86, 88).

On March 1, 1945, the new Contracting Officer

issued findings of fact on respondent's two claims, pointing out that the total of both claims, "the $2,286,819.95 which Bell had charged on its books against CPFF contracts did not, in fact, represent costs of performing such CPFF contracts," that "the costs in question were in fact recovered by [respondent] through the fixed-price contracts" and that "reimbursement for such costs under the CPFF contracts would result in Bell's receiving double payment from the Government" (R. 88-89). The finding concluded that respondent was not entitled to reimbursement under its CPFF contracts "for any portion of the said sum of $2,286,819.95" (R. 89).

On respondent's appeal under Article 16 of the CPFF contracts (the general Disputes article) from that portion of the Contracting Officer's findings which denied the $980,000 claim, the War Department Board of Contract Appeals affirmed (R. 89-91). Recognizing that reimbursability of the claimed costs depended on examination of "all of the circumstances and facts involved" the Board stated:

> * * * The subject costs—both engineering and development, and production tooling costs —were incurred a considerable time before any of the CPFF contracts were entered into. The production tooling costs were incurred for the express and admitted purpose of performing certain fixed-price contracts then on hand or in process of negotiation. They were not incurred in anticipation of the CPFF contracts

and would have necessarily been incurred regardless of whether any further contracts for the P-39 type of airplane were received or not. The engineering and development costs were incurred during the period 1938 to 1940 and the costs were capitalized because it was felt that the development in connection with which they were incurred had a probable value in connection with expected future sales. In 1940 [respondent] entered upon a course of conduct by which these costs were charged against certain fixed-price contracts. The procedure of charging these costs against fixed-price contracts was continued during 1941 and 1942 in accordance with the mentioned plan to the effect that at the end of 1942 all of the costs in question had been absorbed. During this period some of the subject CPFF contracts were entered into and all of them were negotiated prior to August of 1943 at which time [respondent] changed its plan of amortization to the one now contended for. It is clear from the record that no portion of these costs was included in the estimates under the CPFF contracts and no specific consideration was given to the question of reimbursement in the negotiation of the subject contracts. It also may be reasonably concluded that [respondent] had no intention, at the time the contracts were entered into, of seeking reimbursement for such costs since its accounting method did not contemplate reimbursement.

* * * * *

> Under these circumstances it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated, [respondent] did not intend that the item should be reimbursable and was in fact charging the costs in question against other contracts in accordance with a previously adopted plan. The contracting officer in effect has found that the costs in question were in fact recovered by [respondent] through the fixed-price contracts. Although [respondent] states that these costs were not specifically set out as such in the quotations on the fixed-price contracts, it produced no evidence that these costs were not in fact recovered under the fixed-price contracts. Under the circumstances here present, the Board is of the opinion that the costs are not reimbursable under the subject contracts.

Respondent took no appeal from the Contracting Officer's ruling on the 1¼ million dollar claim, which had theretofore been paid but recouped (R. 89).[5]

[5] Respondent objects to our statement that it "took no appeal" from the ruling on the 1¼ million dollar claim on two grounds: (1) the Court of Claims found that the Contracting Officer "did not act upon" that claim, and (2) the Board of Contract Appeals limited its decision to the $980,000 claim (Brief in opposition, p. 5). The short answer to the first ground is that the court made no such finding. Instead it viewed the Contracting Officer's action on the 1¼ million dollar claim as being "without any effect" (R. 115), a view with which we disagree (see *infra*, pp. 35-41), but which in any event assumes that action *was* taken by the officer as to the 1¼ million dollar claim. Nor is it possible for us to see how the second ground advanced by respondent in any way justifies

Respondent then brought the instant suit in the Court of Claims, demanding payment of the 1¼ million dollar claim and of the $980,000 claim. The court concluded that respondent was entitled to recover the full amount of both claims and awarded judgment for $2,286,819.95 (R. 101, 135). Chief Judge Jones and Judge Madden dissented (R. 132, 133). Judge Jones agreed that respondent was entitled to recover on the 1¼ million dollar claim, but stated that he would disallow the $980,000 claim (R. 132). Judge Madden pointed out that it was "beyond question" that the parties intended "that the costs here sued for were not to be reimbursable" under the CPFF contracts, and that, accordingly, respondent's "recovery is a complete and unexpected windfall of $2,286,819.95." (R. 134). He was therefore of the opinion that recovery should have been denied on both claims (R. 135).

SPECIFICATION OF ERRORS TO BE URGED

The Court of Claims erred:

1. In holding that the issue of cost reimbursability was one of law rather than of fact.

2. In failing to hold that the provisions of Article 16 of the CPFF contracts made the determination of the Board of Contract Appeals final and conclusive as to the $980,000 claim.

3. In holding that it had authority to review the determination of the Board of Contract Appeals as

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its failure to appeal that ruling. It was precisely that failure to appeal which forced the Board to limit its decision to the $980,000 claim.

to the $980,000 claim, to set it aside, and to substitute its own judgment for that of the Board.

4. In holding that Article 3(b) of the contracts, which authorized the contracting officer to pass upon the reimbursability of claimed costs, made the first contracting officer's approval of the 1¼ million dollar claim final and conclusive against the Government.

5. In holding that an Article 3(b) determination by a contracting officer against the contractor is not final and conclusive as to the contractor but that such a determination in his favor and against the Government is final and conclusive as to the Government.

6. In holding that the ruling of the second contracting officer as to the 1¼ million dollar claim was without any effect on respondent.

7. In holding that respondent's failure to appeal that ruling did not bar suit on the 1¼ million dollar claim.

8. In holding, on the merits of the controversy, that the deferred charges in question constituted allowable items of cost and that reimbursement of such costs was required under the CPFF contracts.

9. In entering judgment for respondent for $2,286,819.95.

SUMMARY OF ARGUMENT

The "finality" provision of the disputes clause of the standard CPFF government contracts here involved makes the decision of the head of the department final and conclusive as to all factual disputes arising under the contracts. Obviously, a

main purpose of the "finality" provision is to avoid expensive, time-consuming litigation.

This purpose has been frustrated in the past by the Court of Claims' refusal to apply the plain requirements of the "disputes" clause. It is that same refusal which accounts for the basic error of the court in the instant case.

I

In endeavoring to escape the impact of the "finality clause," at least as to the $980,000 claim, the court below labelled the disputed issue as one of law. The matter in dispute was whether the deferred experimental, development and tooling costs were in fact incurred as a necessary incident to the performance of the CPFF contracts. The answer to this question depended on such issues as when the charges were incurred, whether they had to be incurred to complete the earlier fixed-price contracts, whether they had already been amortized against fixed-price plane production, and whether the estimates of costs for the CPFF contracts included these charges.

That these questions were factual is plain both as an original matter and under well-established principles. It is settled that claims involving the ascertainment of cost pose inquiries of fact. Similarly, it has uniformly been held that the issue as to whether a certain charge is a necessary business expenditure is essentially factual. These principles are decisive here and compel the conclusion that the question involved is one of fact.

The only possible question of law before the court below was whether respondent's reallocation of the deferred charges on its books to CPFF production as well as fixed-price production automatically entitled it to reimbursement for the portion of those charges so assigned to CPFF production. The court's ruling that the reallocation compelled reimbursement was erroneous. The ruling ignored the difference between the permissibility and the reimbursability of a claimed cost. Consideration of that distinction shows that reimbursement of a permissible cost is not mandatory but depends on evaluation of the particular factual circumstances involved.

II

Since the issue involved was factual, the denial of the $980,000 claim resulted in a dispute covered by the "finality" clause. The finality and conclusiveness of an administrative determination under the "disputes" articles can be set aside only if it is shown that the determination was founded on fraud. No such showing was even attempted here. The court below therefore committed plain error in setting aside the administrative determination of the Board of Contract Appeals as to the $980,000 claim.

III

The court also erred in refusing to hold that respondent's failure to take the administrative appeal provided by the contracts was fatal to its 1¼ million dollar claim.

While payment on that claim was initially allowed, its recoupment precipitated a dispute. When the second contracting officer later ruled that no portion of the deferred charges, including the 1¼ million dollar claim, was reimbursable, the appeal mechanism of the disputes article was the only means through which the respondent could seek relief. Respondent's failure to invoke the appellate procedure so provided destroyed its right to bring suit on the 1¼ million dollar claim.

The court sought to justify respondent's failure to appeal by contending that the initial approval of the 1¼ million dollar claim by the first contracting officer was conclusive against the Government and that the second contracting officer's ruling on the claim was without effect. That contention has no merit. No language in Article 3(b) of the contracts is susceptible of a construction which would accord finality to approvals of payment made thereunder. Nor was there at the time of initial approval or payment any "dispute" which could have brought the "finality" provisions of Article 16 into operation. Furthermore, "finality" clauses are designed to avoid time-consuming review by the courts. They cannot stand in the way of administrative correction of an administrative error. That was all that was accomplished when the second contracting officer recouped and ruled that the 1¼ million dollar claim was not reimbursable. It was then that a dispute first arose and the "finality" pro-

visions of the disputes article were brought into play.

IV

The foregoing errors of the court below are, we believe, dispositive of the case. We also submit that on the merits of the controversy the determination by the second contracting officer and the Board of Contract Appeals that the deferred charges were not reimbursable was correct and that the court's conclusion to the contrary was erroneous.

Reimbursability depended on the relationship between the claimed charges and the CPFF contracts under which they were claimed. The claimed charges were all incurred and set up on respondent's books before any of the CPFF contracts were awarded. They were all originally charged off exclusively against planes produced under the fixed-price contracts. They were never included in the cost estimates submitted in negotiating for the CPFF contract. At the time of these negotiations respondent never intended that it would be reimbursed under the CPFF contracts for any portion of the already-incurred and deferred charges. These considerations underscore the fact that the deferred charges could not reasonably be viewed as necessary or incidental to the performance of the CPFF contracts. Accordingly, the decision of the court below gave respondent, as Judge Madden observed, "a complete and unexpected windfall of $2,286,819.95" for the two claims

on which it was not entitled to recover anything at all.

ARGUMENT

The "finality" clause in Article 16 of each of the CPFF contracts here involved provides that all disputes concerning questions of fact shall be decided by the government contracting officer, with the right of appeal to the head of the department or his representative "whose written decision * * * shall be final and conclusive upon the parties." (Appendix, infra, p. 55.) The same "finality" provisions are incorporated in Article 15 of the standard form government contract. That Article and others having equivalent provisions have been before this Court and have been upheld more than a dozen times. *United States* v. *Wunderlich*, 342 U.S. 98; *United States* v. *Moorman*, 338 U.S. 457; *United States* v. *Holpuch Co.*, 328 U.S. 234, 236; *United States* v. *Beuttas*, 324 U.S. 768, 770; *United States* v. *Blair*, 321 U.S. 730, 734; *United States* v. *Callahan Walker Constr. Co.*, 317 U.S. 56, 58; *United States* v. *McShain, Inc.*, 308 U.S. 512, 520; *Merrill-Ruckgaber Co.* v. *United States*, 241 U.S. 387, 393; *Plumley* v. *United States*, 226 U.S. 545, 547; *Chicago S.F. & C.R. Co.* v. *Price*, 138 U.S. 185, 195; *Martinsburg & P.R. Co.* v. *March*, 114 U. S. 549; *Sweeney* v. *United States*, 109 U.S. 618, 620; *Kihlberg* v. *United States*, 97 U.S. 398, 402.

The prime error of the court below was its refusal, contrary to the teaching of these decisions, to accord to the finality provisions the meaning and content which the parties to the contracts must be

assumed to have intended. In nullifying the conclusiveness of the administrative determination adverse to respondent as to the $980,000 claim, the court reasoned that the "finality" clauses were limited to disputed questions of *fact*, that the question at issue was one of law, and that the claim was therefore not affected by the clauses but subject to judicial reexamination. Nevertheless, the court ruled that the initial administrative action favorable to respondent on the 1¼ million dollar claim with respect to the same question was conclusive against the United States.

These inconsistent views in no way justify the court's awarding respondent recovery on either of the two claims, because:

(1) The contracting officer's denial of the $980,000 claim resulted in a dispute. Since the matter in dispute clearly concerned a question of fact—whether the deferred charges were in fact incurred as a necessary incident of production under the CPFF contracts—Article 16 made the Board of Contract Appeals' resolution of that dispute in favor of the United States conclusive and immune from judicial review.

(2) The first contracting officer authorized payment of the 1¼ million dollar claim when there was no dispute which brought Article 16 into operation. His authorization was therefore not binding but subject to correction by the second contracting officer, whose rejection of the claim must be deemed the resolution of a dispute which brought the "finality" clause into play.

We also show that even if the question be viewed as one which the Court of Claims was free to consider, its decision was palpably wrong and should be corrected here.

I

The Dispute Concerned a Question of Fact

The court below expressly held that the issue of cost reimbursability was one of law and "not one of fact" and therefore not within the finality clause of the disputes article (R. 121). But, notwithstanding this express holding in one portion of its opinion (R. 121), the court below stated elsewhere in the same opinion that the contractor's dissatisfaction with a contracting officer's determination of this issue "would result in a dispute to be resolved by the means provided in the Disputes article of the contract" (R. 111). Since that article, as the court recognized, could be brought into operation only where a question of fact was involved, it is apparent that the court's statement that the contractor had access to the appeal procedure provided by that article necessarily assumed that the issue involved was factual rather than legal.

We submit that this assumption, rather than the court's inconsistent holding to the contrary, was correct. Although the difference between questions of fact and law is not easy to define or apply, our task here is lightened by analysis of what the instant dispute did and did not involve. The conclusion compelled by that analysis is that the only disputed questions were factual. This conclusion is

strongly supported by the uniform holdings of this Court and other courts and by the rulings of the Board of Contract Appeals with respect to claims for reimbursement under similar CPFF contracts.

A. THE NATURE OF THE QUESTION IN DISPUTE SHOWS THAT IT IS FACTUAL

It is conceded that the CPFF contracts do not bar reimbursement of experimental, development and production tooling expenses. That "costs of this type may properly be allowed as reimbursable items" was fully recognized in the decision of the Board of Contract Appeals in this case (R. 90). There was therefore never involved in the dispute, any question as to the scope or interpretation of the contractual provisions authorizing reimbursement Art. 3(b), Appendix, *infra*, p. 51), or of the regulations (T.D. 5000, 26 C.F.R. 26.9(a), Appendix, infra, p. 52), which the contract incorporated by reference.[6] But whether those provisions authorized reimbursement of the particular claimed costs depended on whether the costs were "incident to and necessary for the performance" of the CPFF contracts in question (T.D. 5000, 26 C.F.R. 26.9(a), Appendix, *infra*, p. 52).

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[6] The Treasury Department Regulations contained in T.D. 5000 were promulgated pursuant to the Vinson-Trammel Act of March 27, 1934, as amended by the Acts of June 25, 1936, April 3, 1939, and June 28, 1940 (48 Stat. 505, 49 Stat. 1926, 53 Stat. 560, 54 Stat. 677; 50 U.S.C. App. 1153). These statutes limited profits on sales to the Government of Army and Navy vessels and aircraft. The regulations contained detailed provisions for determining reimbursability of costs incurred by contractors making such sales (Appendix, *infra*, pp. 52-54).

Accordingly, the allowability of the experimental, development and production tooling costs depended on whether as a matter of fact they were incurred as a necessary incident to performance of the CPFF contracts under which they were claimed. That was what was in dispute and nothing more. To answer that question it was necessary to inquire into "all of the circumstances and facts involved" (R. 90): When were the costs incurred? Were they incurred before or during performance of the CPFF contracts under which they were claimed to be necessarily incident? Was the purpose for which the costs were incurred the fulfillment of earlier fixed-price contracts with the Air Corps and Great Britain? Or were they incurred in anticipation of the later award of the CPFF contracts? Would these costs have been incurred by respondent for the purpose of fulfilling the fixed-price contracts even if no CPFF contracts had ever been granted? How were the costs treated on respondent's books? Were they charged to the costs of airplanes delivered under the fixed-price contracts even after some of the CPFF contracts had been negotiated? Did the estimates of cost for the CPFF contracts include these expenses?

There can be no doubt that inquiries of this sort, all of which had to be answered to determine whether the costs were incurred as a proper incident to the CPFF contracts, pose questions of fact and not of law. In resolving these questions the Board of Contract Appeals found that all of the claimed costs were incurred a considerable time

before any of the CPFF contracts were entered into; that they were incurred for the express purpose of performing certain fixed-price contracts rather than any of CPFF contracts; that it was necessary for respondent to incur these costs to produce the planes under its fixed-price contracts; that respondent would therefore have incurred the costs even if no CPFF contracts had been awarded; that all of the costs had been charged by respondent against its fixed-price contract deliveries even after the CPFF contracts had been negotiated; that, at the time of those negotiations, it was not intended or contemplated that the costs would be reimbursed under the CPFF contracts; and that no portion of these costs was included in the estimated cost of producing planes under the CPFF contracts (R. 90-91). Respondent does not dispute these findings. (R. 125).

These factual considerations show that the costs were not incurred as a necessary incident of CPFF contract performance and "did not, in fact, represent costs of performing such CPFF contracts" (R. 89). At the same time these considerations establish the essentially factual nature of the question in dispute.

B. CONSISTENT HOLDINGS BY THE COURTS AND ADMINISTRATIVE AGENCIES CONFIRM THE VIEW THAT THE QUESTION IS FACTUAL

The question as to whether costs were necessarily incurred for the production of the CPFF contracts is simply one aspect of ascertaining the cost of performance under the contract. This Court has held

that claims involving "merely the ascertainment of the cost" are "inquiries of fact" and has accordingly reversed the judgments of the court below in other cases in which that court has attempted to escape the impact of the "finality" clause by labelling purely factual questions as issues of law. *United States* v. *Callahan Walker Co.*, 317 U.S. 56, 61; see also *United States* v. *Wunderlich*, 342 U.S. 98. There is no valid basis for distinguishing the issue in those cases from the cost ascertainment issue here.

An additional persuasive analogy is furnished by the uniform decisions dealing with the question as to whether an expenditure is a necessary business expense and therefore deductible for income tax purposes under Section 23(a)(1)(A) of the Internal Revenue Code. That question normally presents "pure questions of fact". *Commissioner* v. *Heininger*, 320 U.S. 467, 475; *McDonald* v. *Commissioner*, 323 U.S. 57, 64-65; *Peerless Stages* v. *Commissioner*, 125 F. 2d 869 (C.A. 9); *Missouri-Kansas Pipe Line Co.* v. *Commissioner*, 148 F. 2d 460 (C.A. 3); *Chester Distributing Co.* v. *Commissioner*, 184 F. 2d 514 (C.A. 3); *City Ice Delivery Co.* v. *United States*, 176 F. 2d 347 (C.A. 4). The reason for these consistent holdings is obvious. The question normally turns on whether the claimed expense is reasonably and proximately related to the business. *Trust of Bingham* v. *Comm'r*, 325 U.S. 365, 370. Questions of reasonableness and proximity are traditionally regarded as questions of fact. *McDonald* v. *Commissioner*,

323 U.S. 57, 64-65; see *Commissioner* v. *Swedish American Investment* Co., 323 U.S. 119, 124-125.

That reasoning is fully applicable here. The decision that certain costs were not incurred as a necessary incident to the business of performing the CPFF contracts is a decision that the claimed costs did not bear the necessary proximate relation to those contracts. It is a decision, in other words, resolving a factual dispute. The factual nature of similar disputes arising under CPFF contracts has been regularly recognized by the Board of Contract Appeals. *Northrop Aircraft, Inc.*, 3 CCH Contract Cases Fed. 1273, 1274 (appeal taken by CPFF contractor from contracting officer's denial of claimed cost held to be an appeal taken "in accordance with the provisions of the 'Disputes' article (Art. 16) of the contract, which provides for appeal on disputed questions of fact"); *United Air Lines, Inc.*, 3 CCH Contract Cases Fed. 1497, 1500 (reimbursability depends on whether costs "were incident to and necessary for the performance of the contract"); *Douglas Aircraft Company, Inc.*, 3 CCH Contract Cases Fed. 1570, 1571 (after "consideration of all facts and circumstances" the Board denied reimbursability for certain expenses which "may have been of benefit to the Government" but were not "necessary for or incidental to the performance" of the CPFF contracts); *Chrysler Corporation*, 1 CCH Contract Cases Fed. 162 (Board denied reimbursement of claim as not being necessary incident of performance under CPFF contract which stated that disagreements as to re-

imbursability shall be deemed disputes concerning questions of fact within the meaning of Article 16).

The only question of law possibly present in this case is whether the terms of the contract compelled reallocation of the deferred charges to both CPFF contract production and fixed-price production whenever respondent so desired and therefore compelled reimbursability of the portion allocated to the former production. The court below was of the view that the language of T.D. 5000, incorporated into Article 3(b), was mandatory and demanded this reallocation. It ruled that if the costs were allowable there existed the duty of "approving them for reimbursement." (R. 111). It evidently considered that if the costs "fall within the category" (R. 125) which T.D. 5000 makes allowable, they must be allowed. See, generally, R. 124-128.

That this ruling was erroneous can readily be shown. The language of T.D. 5000 makes it clear that an admittedly allowable or permissible cost is not necessarily reimbursable. A cost is permissible when it is of a type which is recognized as generally coming within the category of costs listed by T.D. 5000. If it meets that test the cost *may* be allocated to CPFF production. Whether it should be so allocated, however, depends, as T.D. 5000 provides, on a "complete showing of all pertinent facts." T.D. 5000, 26 C.F.R. 26.9(d), Appendix, *infra*, p. 54. See *Determination of Cost in Military Procurement Cost-Plus-A-Fixed-Fee Contracts*, 65 Harv. L. Rev. 1035, 1039. The Board of Contract Ap-

peals accordingly declared in this case that although "it is true that costs of this type may properly be allowed as reimbursable items under T.D. 5000, it does not follow that such costs must be reimbursed under T.D. 5000 in all cases and under all circumstances. In order to determine whether such items of cost should be reimbursed it is necessary to examine all of the circumstances and facts involved" (R. 90). And, as we have shown at pages 25-27, *supra*, all of the facts involved here show that reimbursement should not be allowed.

It is apparent from the foregoing that the only possible question of law before the court below was incorrectly decided by it, and that a correct disposition of that question confirms our view that determinations as to reimbursability under CPFF contracts of the costs involved here rest essentially on evaluation of the particular factual circumstances involved.

II

The Board of Contract Appeals' Determination of the $980,000 Claim Is Therefore Final and Binding

Since the question was factual, the contracting officer's denial of the $980,000 claim resulted in a dispute covered by the "finality" clause of Article 16 of each of the CPFF contracts.[7] The meaning and effect of that Article is no longer open to doubt. This Court has recently held that the provision for final and conclusive departmental determination

[7] Respondent's brief below admits that its appeal from the denial of this claim "was taken under Article 16 of the Contracts, the 'disputes' clause" (Plaintiff's Brief, No. 47745, Court of Claims, p. 151).

of factual disputes must be given full effect unless the determination "was founded on fraud, alleged and proved." *United States* v. *Wunderlich*, 342 U.S. 98, 100. The Court there emphasized that the only "exception to the conclusiveness of such administrative decision" is fraud on the part of the government arbiter and that "absent fraudulent conduct" his decision "must stand under the plain meaning" of the finality clause of the contract. 342 U.S. at 99, 100. And, to make absolutely clear the scope of the exception to conclusiveness the Court defined fraudulent conduct to "mean conscious wrongdoing, an intention to cheat or be dishonest" (342 U.S. at 100).

Respondent's petition in the court below makes no claim that the denial of the $980,000 claim by the contracting officer or the Board of Contract Appeals was motivated by fraud or an intention to cheat or be dishonest (R. 1-16). To the contrary, respondent made it clear in the court below that it did "not mean to impugn the actual honesty and good faith of any of [the government's] agents. It [*i.e.* the respondent] is prepared to concede that everyone tried to do his duty, honestly and in good faith" (Plaintiff's Brief, No. 47745, Court of Claims, p. 148). In view of this concession by respondent the court below did not and could not find any fraud on the part of the government arbiters.[8]

[8] The majority of the court below did attempt to avoid the impact of the "finality" clause by treating the question as one of law as to which the "disputes" article was inapplicable (R. 121). However, the reasons we have already set out demonstrate that the question was factual in nature. (See *supra*, pp. 25-31.)

There being no fraud, the *Wunderlich* decision requires that the departmental determination at least as to the $980,000 claim "must stand as conclusive." *United States* v. *Wunderlich*, 342 U.S. 98, 101. In refusing to consider itself bound by that determination we submit that the court below plainly erred.

III

The Second Contracting Officer's Unappealed Determination of the 1¼ Million Dollar Claim Is Likewise Final and Binding

In Points I and II we have shown that the issue involved was factual and that the Court of Claims therefore erred in refusing to consider itself bound by the Board of Contract Appeals' denial of the $980,000 claim. We also believe that the court erred in refusing to accord finality to the second contracting officer's unappealed ruling as to the validity of the 1¼ million dollar claim.

The issue involved as to this claim was identical in all respects to that involved in the $980,000 claim, *i.e.*, whether the claimed costs were incurred as a necessary incident to the performance of the CPFF contracts. The issue was, therefore, one of fact as to both claims.[9] Consequently, we agree that an administrative determination of that issue of fact,

[9] Respondent brushes aside the inconsistencies in its arguments, adopted by the Court of Claims (*supra*, p. 24), by accusing the Government of urging that the issue before the first contracting officer was one of law and that before the second was one of fact (Brief in Opposition, pp. 16-17). We have never advanced any such inconsistent position. On the contrary, in this Court as well as in the court below (R. 117) our basic position has always been that the issue before both officers and before the Board of Contract Appeals was purely factual.

if made under the disputes provisions of the contracts, would be entitled to finality and would be unreviewable by the courts. This does not mean, however, that the allowance of the 1¼ million dollar claim by the first contracting officer is conclusive here: (1) that allowance was not a resolution of a "dispute" within Article 16; (2) nothing in Article 3(b) purported to give finality to such an allowance; and (3) in any event, "finality" provisions, while precluding judicial review, do not prevent administrative correction of administrative errors. It was permissible, therefore, for the second contracting officer to rectify the initial approval through recoupment and to disallow the 1¼ million dollar claim. That action resulted in a dispute within the meaning of Article 16 and respondent's failure to appeal made the disallowance final and conclusive.[10]

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[10] As early as June 1944, respondent was put on notice, through copies of letters furnished by the Resident Auditor for the Army Air Corps, that it was intended to recoup the moneys paid respondent on the 1¼ million dollar claim by deducting that amount from payments due respondent on other vouchers (R. 87). The Resident Auditor's action in recommending the deduction on the vouchers was of course subject to review by the contracting officer and to whatever action "he saw fit". (Transcript, pp. 403-404, 426). And the record shows that in reviewing the recommended deductions the contracting officer took specific action in September, 1944, to correct the erroneous allowance of the 1¼ million dollar claim by "approv[ing]" these vouchers "for recoupment." (Transcript, p. 440). After taking this action, the contracting officer transmitted to the Finance Officer for settlement "the vouchers on which deductions were made by the Resident Auditor" (R. 87; Transcript, p. 440).

A. THE FIRST CONTRACTING OFFICER'S INITIAL APPROVAL OF THE 1¼ MILLION DOLLAR CLAIM WAS NOT CONCLUSIVE

1. *The express terms of Article 16 show that the first Contracting Officer's approval was not a decision under Article 16.* Article 16, which is entitled "Disputes", declares that "all [factual] *disputes*", not disposed of by mutual agreement, "shall be decided by the Contracting Officer", from whose decision the departmental determination on appeal shall be final. (Emphasis supplied). Thus, the basic condition for bringing Article 16 into play is the existence of a dispute. A dispute exists only where something asserted on one side is denied by the other. *In re Robinette*, 211 Minn. 223, 300 N.W. 798. There can be a dispute only where there is controversy, disagreement, opposing contentions or argument to persuade the other side to change its position. *Miners' General Group* v. *Hix*, 123 W. Va. 637, 643-644, 17 S.E. 2d 810, 814; *Block Coal & Coke Co.* v. *United Mine Workers*, 177 Tenn. 247, 148 S.W. 2d 364. Where a claim is filed and rejected it is obvious that a disagreement or dispute has resulted. *Leyerly* v. *United States*, 162 F. 2d 79 (C.A. 10); *Shaull* v. *United States*, 161 F. 2d 891 (C.A. D.C.); *Thrasher* v. *United States*, 132 F. 2d 747 (C.A. 5); *Johnson* v. *United States*, 102 F. 2d 729 (C.A. 10). It is equally apparent that where a claim is filed and acquiesced in by the other side so that payment of the claim is immediately forthcoming no dispute can be said to exist.

Nothing more than that happened here with respect to payment of the 1¼ million dollar claim.

While there was an adverse recommendation by the Assistant Resident Auditor, his recommendation was overruled by his superior, the Resident Auditor, who certified the vouchers to the Contracting Officer, who, in turn, approved them for payment without voicing any objection. There was never any controversy or dispute, therefore, between the respondent and the United States with respect to the initial allowance of that claim.[11]

The foregoing reasoning has been consistently applied to prevent any finality from attaching under Article 16 to an officer's approval for payment in the absence of a dispute. In passing on this question in a similar CPFF contract case, the Office of Contract Settlement Appeal Board recently observed:

> It remains to consider whether the disputes article renders approval of the propriety of the payments by the contracting officer final and conclusive. In my opinion, it has no such effect. In order to bring the disputes article into play, a dispute must exist. Very probably if the contracting officer had disallowed the [claims] * * * and appellant had succeeded in getting him to pass them there would have been a determination binding and conclusive on the parties under the disputes article. * * * In the absence of a dispute, however, the disputes article is without force or effect. [*Her-*

[11] As a matter of fact, there is no evidence that the first Contracting Officer was even aware of the divergent views of the Resident Auditor and the Assistant Resident Auditor.

cules Powder Co. v. *Army*, 4 OCSAB Cases 94, 99-100 (No. 326, Jan. 26, 1950).]

The mere approval of a payment of a claim under a CPFF contract cannot therefore be deemed a conclusive and binding determination. *Hercules Powder Co.* v. *Army, supra; Northwest Airlines, Inc.* v. *Army*, 4 OCSAB Cases 20, 23-24 (No. 282, July 15, 1949); *Hudson Motor Co.* v. *Navy*, 2 OCSAB Cases 39 (No. 134, Aug. 7, 1947); see also *Hercules Powder Co. v. Army*, 4 OCSAB 218, 221, 222 (No. 333, June 14, 1950).

Apart from the "dispute" requirement, other language in Article 16 shows that the contracting officer's initial approval of the claim was not tantamount to a decision under that Article. Three of the four CPFF contracts require the Contracting Officer to "reduce his decision [of any dispute] to writing" and "to mail a copy thereof" to the contractor.[12] Since the Contracting Officer, in approving the vouchers submitted on the 1¼ million dollar claim, did not decide any dispute, there was nothing for him to reduce to writing or to mail to

[12] These requirements appear in Article 16 of Contracts numbered W. 535 ac-20910 (R. 19-20), W. 535 ac-29318 (R. 28) and W. 535 ac-40071 (R. 33). The text of Article 16 of each of these contracts is set forth as exhibits to the petition filed below (R. 19-20, 28, 33). Contrary to the finding of the court below (R. 80, 81), the short-form version of Article 16, which did not require the Contracting Officer's decision to be in writing but which did require the existence of a dispute, appears only in Contract No. W. 535 ac-156 (R. 25). And, even the short-form version, though not expressly requiring a written decision, must, in order to make effective the contractor's right of appeal, be construed to require that the contractor be served with notice of the contracting officer's decisions. (R. 25.)

respondent. If any dispute had been decided at that time, it is fair to assume that these requirements of Article 16 would have been observed.

2. *Nothing in Article 3(b) of the contracts makes the first Contracting Officer's initial approval final and conclusive.* Article 3(b) states that "allowable items of cost will be determined by the contracting officer" (R. 18, 23, 26, 30). All that this language does is to authorize the Contracting Officer, rather than anyone else,[13] to determine the permissibility of claimed costs under the CPFF contracts. The Court of Claims nevertheless read this language so as to make "conclusive and binding" against the Government any determination under Article 3(b) (R. 111). But there is not a single syllable in Article 3(b) referring to finality. Nor does it have any language from which a finality provision can be implied. The provisions of Article 3(b) "fall far short of the 'final and binding' language" necessary to accord finality to the contracting officer's determination of allowability of a claimed cost. *Northwest Airlines, Inc.* v. *Army*, 4 OCSAB Cases 20, 24 (No. 282, July 15, 1949). Indeed, the court below recognized that no finality attached to an Article 3(b) determination with which the contractor was not fully satisfied. The court observed that the contractor's objection to such a determination "would result in a dispute to be resolved by the means provided in the Disputes

[13] The parties bargained for a determination by the contracting officer (see second paragraph of next footnote, *infra*, p. 42), but not that his decision, once made, should be final and free from revision by himself or his successor.

article of the contract" (R. 111). Certainly, if an Article 3(b) determination can be upset by the contractor's mere objection, by no process of proper reasoning can it be held final and conclusive against the Government.

In holding that an Article 3 (b) determination was binding and conclusive, the court below was apparently influenced by respondent's reliance in that court on *United States* v. *Moorman*, 338 U.S. 457. This Court there held that the contracting officer's determination under Par. 2-16(a) of the specifications was final and binding, whether the question was one of fact or law. But Par. 2-16(a), unlike the Article 3(b) provisions here, stated "in language as plain as draftsmen could use that findings of the Secretary of War in disputes of the type here involved shall be 'final and binding.'" *United States* v. *Moorman*, 338 U.S. 457, 463. For the same reason, *United States* v. *Mason & Hanger Co.*, 260 U.S. 323, 325, is not in point—the Article 4 in the contract in that case, unlike Article 3(b) here, expressly made the cost determination "final and binding." The holding in this case that Article 3(b), despite the absence of any similar language of finality, rendered conclusive against the Government the first contracting officer's initial authorization of payment is therefore in complete disregard of the plain provisions of the contract.

3. *"Finality" clauses are intended to prevent judicial review of administrative action rather than the administrative agency's correction of its own error.* There is still another reason precluding

any holding that the first contracting officer's initial approval of the 1¼ million dollar claim was conclusive against the Government and not subject to correction. Even if the language of either Article 16 or Article 3(b) could possibly be interpreted so as to make his approval final, it is our position that the finality attaching to such a determination prohibits judicial review but not administrative correction of an administrative error.

As early as 1878 the Court observed that the purpose of the "disputes clause" was to avoid subjecting the administrative determination "to the revisory *power of the courts.*" *Kihlberg* v. *United States*, 97 U.S. 398, 401 (italics supplied). By agreeing to such a clause the parties agree to "deprive [themselves] of a right to have their controversies *decided in court.*" *United States* v. *Moorman*, 338 U.S. 457, 462 (italics supplied). The parties, in other words, recognizing that the technical disputes bound to arise under the contract are best and more speedily resolved by administrative determination, agree to such a determination of these disputes and agree to immunize the determinations against expensive, time-consuming court litigation.

With this purpose in mind, it is obvious that the "finality" language may be invoked only for the purpose of preventing judicial reappraisal of an administrative determination. It cannot be resorted to in order to forestall administrative correction of an administrative error. *United States* v. *Bentley*, 107 F. 2d 382 (C.A. 2); *Morgan* v. *Hines*, 113 F. 2d 849, 850 (C.A.D.C.); *United States* v.

Gudewicz, 45 F. Supp. 787 (E.D.N.Y.). In the *Bentley* case, the court stressed the fact that "finality" clauses are "not designed to prevent review of their own decisions by the officials themselves, but to limit any review of the courts." 107 F. 2d 382, 383. The court accordingly rejected the argument that the Secretary of War could not correct an earlier decision made "final and conclusive" by the statute under which it was handed down.

For the same reasons the Department of the Army, in this case, acting through the second contracting officer, was fully empowered to correct the first contracting officer's authorization even if it be assumed, contrary to the contentions we have advanced, that "finality" attached to the authorization either under Article 16 or 3(b). Certainly, if the first contracting officer had denied the claim improperly or had given respondent too little, the second contracting officer would not have been compelled to perpetuate the injustice on the theory that the "finality" language forbade him to correct the earlier mistake. Nor should he be compelled to perpetuate the injustice where, as here, the first contracting officer awarded too much.[14]

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[14] That the Government may, as it did here, recoup moneys paid out by a public officer under mistake of either fact or law is well settled. *United States* v. *Wurts*, 303 U.S. 414; *Wisconsin Central R.R.* v. *United States*, 164 U.S. 190, 212; *United States* v. *Burchard*, 125 U.S. 176; *Heidt* v. *United States*, 56 F. 2d 559 (C.A. 5), certiorari denied, 287 U.S. 601; *United States* v. *Sutton Chemical Co.*, 11 F. 2d 24 (C.A. 4). This proposition is fully applicable even where the administrative action leading to the improper payment is "final and binding." *United States* v. *Bentley*, 107 F. 2d 382 (C.A. 2);

B. SINCE RESPONDENT IGNORED THE AGREED PROCEDURE FOR SETTLEMENT OF DISPUTES, IT HAS NO STANDING TO SUE FOR DAMAGES BASED ON SUCH DISPUTES

There was no dispute between respondent and the Government when the first contracting officer authorized payment of the 1¼ million dollar claim. *Supra*, p. 35. However, approval of vouchers by the second contracting officer providing for recoupment of that payment, which was the equivalent of rejection of the 1¼ million dollar claim, did result in a dispute. Therefore, in his written finding of fact and decision, dated March 1, 1945, the Second Contracting Officer considered this disputed claim as well as the $980,000 claim and decided that respondent was not entitled to reimbursement on either claim (R. 89).

Article 16 of each of the four CPFF contracts provides for decision of disputed factual questions by the contracting officer. His decision, however, is subject to appeal to the head of the department (or his representative) whose decision "shall be final and conclusive." It is now settled that this

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Morgan v. *Hines*, 113 F. 2d 849 (C.A. D.C.); *United States* v. *Gudewicz*, 45 F. Supp. 787 (E.D. N.Y.).

The "finality" clauses, as we have shown (pp. 29-41), do not bar correction by the administrative agency of its own error. Thus, in the instant case, the Department of the Army, acting through the second contracting officer, could correct the first officer's error. This situation must be distinguished from that where the administrative agency insists that no error has been made by it but the General Accounting Office asserts that the payment was improper. See *Mathis Co.* v. *United States*, 79 F. Supp. 703 (D. N.J.), relied on by respondent below. In that situation the courts will not allow the General Accounting Office to substitute its decision for the determination of the administrative agency because the latter determination is the only one by which both parties had contracted to abide.

appeal "mechanism . . . is exclusive in nature. Solely through its operation may claims be made and adjudicated as to matters arising under the contract." *United States* v. *Holpuch Co.*, 328 U.S. 234, 239-240; *United States* v. *Blair*, 321 U. S. 730, 735; *United States* v. *Callahan Walker Co.*, 317 U. S. 56, 61. A contractor who, after accepting and agreeing to Article 16, ignores its provisions "destroys his right to sue for damages in the Court of Claims. That court is then obliged to outlaw his claims, whatever may be their equity. To do otherwise is to rewrite the contract." *United States* v. *Holpuch Co.*, 328 U.S. 234, 240.

Here, respondent complied with the provision of Article 16 as to the $980,000 claim but chose to ignore those same provisions as to the second contracting officer's disallowance of the 1¼ million dollar claim. With respect to the latter claim, therefore, respondent's position is precisely the same as that of the respondents in *United States* v. *Holpuch Co.*, 328 U.S. 234; *United States* v. *Blair*, 321 U.S. 730, and *United States* v. *Callahan Walker Co.*, 317 U.S. 56, all of whom were denied recovery by this Court on the ground that they had failed to take the administrative appeal provided by the "Disputes" article. We submit that the same reasons which impelled this Court to reverse the Court of Claims in the *Holpuch*, *Blair* and *Callahan Walker* cases require reversal as to the 1¼ million dollar claim in the instant case.[15]

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[15] If respondent had appealed, the grounds of decision taken by the Board as to the $980,000 claim would have required

As in the *Holpuch* and *Blair* cases, so here "the Court of Claims sought to justify respondent's refusal" or "failure to pursue the procedure outlined in" the Disputes Article. See 328 U.S. at 242; 321 U.S. at 736. It sought to avoid the effect of the *Holpuch*, *Blair* and *Callahan Walker* decisions on two grounds. First, the court noted that the first contracting officer had authorized payment so that no dispute then arose which brought the Disputes Article into play (R. 116). With that observation we fully agree. See *supra*, p. 35. But it is beside the point. It overlooks the whole thrust of our argument in the court below and here, *i.e.*, that a dispute which did bring Article 16 into play resulted when the claim was disapproved and that payment was recouped. The court's second reason for refusing to apply *Holpuch* and its related cases was that "there was no occasion for the second Contracting Officer to make any findings or render any decision" as to the 1¼ million dollar claim (R. 116). The short answer to this argument is that it does not accord with the facts. The record shows that the 1¼ million dollar claim had been fully recouped by the Government no later than September, 1944 (R. 87-88). Since this claim was never abandoned by respondent it was still outstanding and therefore necessarily before the second con-

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the Board also to deny the 1¼ million dollar claim, and respondent would for that reason have been unable to recover. But since respondent's failure to appeal precluded the Board from considering the 1¼ million dollar claim, it follows that decision against respondent on that claim must be rested on the failure to appeal.

tracting officer when he decided, in March, 1945, that both that claim as well as the $980,000 claim were not reimbursable (R. 89).[16] Accordingly, neither of the grounds relied on by the court below justifies its condonation of respondent's failure to exhaust the administrative appeal remedy afforded by Article 16.

IV

In Any Event, the Determination by the Second Contracting Officer and the Board of Contract Appeals That the Deferred Charges Were Not Reimbursable Was Correct and That of the Court Below Erroneous

In our view, the Board of Contract Appeals' determination of non-reimbursability as to the $980,000 claim and the second contracting officer's unappealed disallowance of the 1¼ million dollar claim are conclusive as to the respective claims and hence dispositive of the present case. It is our further belief that with respect to the merits of the controversy the decision below is also erroneous.

The reimbursability of the deferred experimental development and tooling charges depended, as has been shown, on whether they were incurred as a necessary incident to the performance of the CPFF contracts under which they were claimed (See *supra*, p. 25). In deciding that the charges

[16] The court's opinion also refers to the General Accounting Office's lack of power to reverse the first contracting officer's approval of payment (R. 116). But here the administrative agency itself, *i.e.*, the Army department, acting through the second contracting officer, reversed the earlier decision. It is true that the second contracting officer's view coincided with those of the General Accounting Office. That cannot change the fact that it was the Army itself which corrected its earlier error. See footnote 14, *supra*, pp. 41-42.

were reimbursable the court below implicitly held that they were so incurred. That holding, we show below, has nothing to support it.

The experimental and development costs were incurred by respondent in connection with the four experimental contracts it received in 1936-1938 (R. 67). By the end of 1940, all of these costs, aggregating 1½ million dollars, had been deferred and capitalized on respondent's books (R. 69). It is significant that the first CPFF contract was awarded on August 14, 1941 and that respondent had no CPFF contracts as of December, 1940, when all of the deferred experimental and development costs already had been set up on its books (R. 76).

The claimed tooling costs were incurred by respondent in producing over 1700 P-39 planes for the United States and Great Britain under fixed-price contracts amounting to approximately 70 million dollars. These costs were incurred in 1939 and 1940, so that by the end of 1940 all of the tooling costs, aggregating almost $1,900,000.00, also had been deferred and capitalized on respondent's books. As already noted, there were no planes under CPFF contract at that time. To the extent that any production tooling costs were incurred by respondent after August 14, 1941 and in connection with the CPFF contracts entered into on and after that date respondent has received reimbursement under the CPFF contracts (R. 99; see footnote 4, *supra*, p. 11). It is important to remember that these CPFF tooling costs are not here involved. In the instant suit respondent claims reimburse-

ment under CPFF contracts for the tooling costs it incurred in 1939 and 1940 in order to fulfill the fixed-price contracts it then had (R. 89).

The fact that the deferred charges were all incurred and set up on respondent's books before any of the CPFF contracts were awarded would by itself establish at least a strong *prima facie* case that the charges were unrelated to the later CPFF production and hence not a necessary incident to performance of the CPFF contracts. Here, however, many other factors confirm that conclusion:

1. Respondent originally charged off the entire amount of the deferred charges to planes produced under the fixed-price contracts (R. 76). This process of charging the deferred costs to fixed-price production alone began in 1940 and was continued by repondent through 1942, until by the end of 1942 those costs had been fully allowed from the fixed price contracts. This process was followed despite the fact that, starting in August, 1941, it received a series of CPFF contracts calling ultimately for the production of over 10,000 P-39's (R. 76). If the deferred charges were considered a necessary incident to CPFF contract production it seems obvious that a portion of those charges would, during 1941 and 1942, have been allocated by respondent to CPFF production.

2. That respondent did not consider the charges as a necessary incident to CPFF production and therefore never intended to be reimbursed for such charges under the CPFF contracts is attested to by still other considerations: (a) Respondent's An-

nual Reports for 1941 and 1942 stated that it was its intention to charge off the entire amount of the deferred charges to airplanes under contract as of December 31, 1940 (R. 76). The only aircraft then under contract were those called for by the fixed-price contracts with the Air Corps and Great Britain (R. 71). (b) Respondent never included any portion of the deferred charges in any of its estimates of cost submitted in negotiating for the CPFF contracts (R. 76, 82, 125). And (c) respondent expressly recognized that this failure to include the charges in the negotiations for the CPFF contracts compelled it to amortize these charges "against the fixed price contracts only" and precluded reimbursement for the charges under the CPFF contracts (R. 82).

The fact that respondent's decision to claim reimbursement for these expenses under its CPFF contracts was the result, at least in part, of pressure from the Bureau of Internal Revenue, with respect to excess profits taxes, does not justify the result reached by the Court of Claims. The Bureau had no power to amend the CPFF contracts or to determine what items should be reimbursable under them. Moreover, it is significant that the tax adjustment increased respondent's net tax liability by approximately $32,000, as compared with the amount of $2,286,819.95 here awarded to respondent below (R. 60, 134). Nor can any justification be found in the renegotiation agreement entered into between respondent and the United States for 1942. That agreement did not compute respond-

ent's excessive profits on the basis of allowing a portion of the deferred charges as costs under the CPFF contracts. Instead, it allowed respondent to charge all of the deferred costs to P-39 production under the fixed-price contracts (R. 93-94). The agreement further provided that if the Army and General Accounting Office finally approved reimbursement under the CPFF contracts of the claimed portion of the deferred charges, an additional refund of $667,000 would be required of respondent (R. 94). That final approval, of course, was not granted and the provision has not yet taken effect, and cannot take effect unless this Court affirms the judgment below.

In these circumstances, as the Board of Contract Appeals observed, "it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated, [respondent] did not intend that the item should be reimbursable and was in fact charging the costs in question against other contracts in accordance with a previously adopted plan." (R. 91). Judge Madden's dissent summarizes these considerations by demonstrating that the Court of Claims allowed respondent to recover "for something [for] which, when it made the contracts under which it claims the payment, it intended that it should be paid nothing at all" (R. 133). The court's decision, as Judge Madden further observed, therefore gave respondent "a complete and unexpected windfall of $2,286,819.95" for two

claims on which it was not entitled to recover anything at all.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment below should be reversed.

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SEPTEMBER, 1952

APPENDIX

1. Each of the four CPFF contracts contains the following provisions (R. 18, 23-24, 25-26, 29-30):

ARTICLE 3. CONSIDERATION

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the contract, subject to reimbursement for cost as outlined in Article 6 hereof, the cost, plus a fixed fee of * * * being * * * percent of the total estimated cost of * * *. This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

(b) For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T.D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

(1) All costs which have been incurred by the Contractor in anticipation of this contract

and prior to the signing thereof, and which if incurred after the signing of this contract, would have been considered as allowable items of cost within the meaning of said regulations, shall be considered as allowable items of cost incurred hereunder.

2. The Treasury Department regulations referred to in Article 3 (b) of the contracts *supra*, provide in pertinent part (26 C.F.R. 26.9, 1940 Supp.):

§ 26.9 *Cost of performing a contract or subcontract*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract; and (2) the proper proportion of any indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.

(b) *Elements of cost.*—No definitions of the elements of cost may be stated which are of invariable application to all contractors and subcontractors. In general, the elements of cost may be defined for purposes of the Act as follows:

(1) Manufacturing cost, which is the sum of factory cost (see paragraph (c) of this section) and other manufacturing cost (see paragraph (d) of this section);

* * * * *

(c) *Factory cost.* Factory cost is the sum of the following:

* * * * *

(5) *Indirect factory expenses.* Items, usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

* * * * *

(iv) *Fixed charges and obsolescence.* Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable standby equipment; and depreciation and obsolescence of special equipment and facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the Department concerned has made a certification binding upon the Commissioner of Internal Revenue, pursuant to section 4 of the Act, in the case of such contract or subcontract. * * *

* * * * *

(d) *Other manufacturing cost.* Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs

which are not properly or satisfactorily chargeable to factory costs (see paragraph (*c*) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

* * * * *

3. a. The Disputes Article in the CPFF contract numbered W 535 ac-156 Provides (R. 23, 25):

ARTICLE 16. DISPUTES

> Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance.[17]

b. The Disputes Article in the three other CPFF contracts provides (R. 19-20, 28-29, 33):

ARTICLE 16. DISPUTES

> Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days

[17] Our petition for certiorari, relying on the findings of the Court of Claims (R. 80), stated that this short form version of Article 16 appeared in three of the four CPFF contracts. But the record shows that it appeared in only one CPFF contract and that the longer version of Article 16, set out under 3(b) of the Appendix, appeared in the other three contracts. See record references under 3(a) and 3(b) of the Appendix.

from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. * * * Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

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No. 13

IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

THE UNITED STATES, *Petitioner*,

v.

BELL AIRCRAFT CORPORATION, *Respondent*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR RESPONDENT

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

No. 13

THE UNITED STATES, *Petitioner,*

v.

BELL AIRCRAFT CORPORATION, *Respondent*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR RESPONDENT

OPINION BELOW

The opinion of the Court of Claims (R. 101-35) is reported at 120 Ct. Cl. 398.

JURISDICTION

The judgment of the Court of Claims was entered on October 2, 1951. (R. 135) On December 29. 1951, the Chief Justice extended the time for filing a petition for a writ of certiorari to and including January 30, 1952. (R. 136) The petition, filed on that date, was granted on March 31, 1952. (R. 139) The jurisdiction of this Court is invoked under 28 U.S.C. § 1255(1) (1946).

REGULATION AND CONTRACT PROVISIONS INVOLVED

The pertinent provisions of the regulations and contracts involved in this case are set forth in Appendices A and B, *infra* at pp. 73-88.

STATEMENT OF THE CASE

Bell Aircraft Corporation, the respondent, was the designer and builder of the P-39 fighter airplane of World War II fame—the Airacobra. The issue in this case is respondent's right to reimbursement from the petitioner for some $2,286,000 of costs incurred in connection with development and production of that plane. Resolution of that issue requires some understanding of the technical and procurement problems involved in United States military aviation before and during World War II, and the manner in which they were solved.

The events with which the controversy is concerned date back almost to the formation of respondent with three employees in 1935. (Tr. 125-26)[1] Within a year thereafter, respondent undertook to solve some of the peskiest problems of military aviation of that day through development of a new type of fighter airplane with adequate nose room and pilot vision, with the fire power of a true cannon and with efficient use of the important new Allison liquid-cooled engine. (R. 67-69, 95-98)[2]

Development of a new type craft was a risky and costly business. The most perfect calculation and design going into the drawings gave no reliable clue as to costs of production and no assurance of successful per-

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[1] As has the petitioner in its brief, we shall occasionally cite portions of the certified record not printed by the petitioner.

[2] The respondent's success in securing a craft with a long drive shaft and adequate nose room, and in solving certain shimmy problems with respect to the guns, led directly to the development of the revolutionary tri-cycle landing gear in the Airacobra. (R. 96, Tr. 49-51)

formance.[3] Hence, typically, the military first would order construction of hand-made, purely experimental planes. If all went well, the military would then order construction of a limited number of test craft of that type, still experimental and intended to provide the means for critical and exhaustive testing. If all then finally went well, the military would order the plane into production. At that point the aircraft company would outfit assembly lines and tool up for quantity manufacture. For this purpose so-called "production tools" were necessary, not ordinary machine tools but special structures and devices, usable only in the production of that type of craft, such as fixtures designed to hold portions of the aircraft exactly in place during fabrication. (R. 72)

In the system of letter-number designations used in military aviation, the prefix "X" designated the hand-made experimental planes. The prefix "Y" designated the test models. (R. 67) Upon regular production such prefixes were dropped.

Difficult as it was in the case of ordinary production to forecast aircraft costs, it was quite out of the question to forecast the costs of constructing the experimental craft;[4] nor would the military have any way

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[3] The impracticability of letting contracts on the basis of drawings alone has always been a complicating factor in aviation procurement. See Statement of Maj. Gen. E. M. Powers, Assistant Chief of Air Staff, *Hearings Before Subcommittee No. 6 of the House Committee on Armed Services on H. R. 1366*, 80th Cong., 1st Sess. 536 (1947); 1 ASF, Purchasing Policies and Practices, Official History of Purchases Division 22. This undated mimeographed manuscript is on file with the Historical Division, Department of the Army.

[4] H. R. Rep. No. 1634, Part 1, 77th Cong., 2d Sess. 233 *et seq.* (1942); Major Davidson Sommers, *Cost-Plus-Fixed-Fee Contracts*, 2, 13 (1944) (lecture presented at AAF Contracting Officers School, Wright Field, Dayton, Ohio, on file at the Army Library).

of appraising the value to it of such construction. Hence, in aircraft manufacture, a fixed price contract let for experimental production was simply a device whereby the military would defray a portion of the cost of the experiment. The excess of the manufacturer's costs over the military's payment would constitute what cost accountants denominate "experimental and development" or "e and d" costs, to be amortized over the production, if any, of the aircraft to which the experimental and developmental work was related.[5]

Upon reaching the production stage, the job of contracting took on a different character. Especially in the days when France was crumbling and England was tottering, it was impossible for either the military or the manufacturer to make predictions with certainty. A contract for a limited number of planes would be let; it would *probably* be followed by others; but obviously no one could tell how many others or when or in what quantities.[6] Furthermore, especially where the type

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[5] See General Arnold, *Hearings before Subcommittee of the House Committee on Appropriations on the Military Establishment Appropriation Bill for 1940*, 76th Cong., 1st Sess. 315 (1939).

[6] Lilley, Hunt, Butters, Gilmore, Lawler, Problems of Accelerating Aircraft Production During World War II 15, 22-30 (1946); John Perry Miller, Pricing of Military Procurements 20 (1949); John W. Fesler, Industrial Mobilization for War: History of the War Production Board and Predecessor Agencies 40, 47-50, 55-56, 121, 126 (1947); Joseph Carlyle Sitterson, Aircraft Production Policies Under the National Defense Advisory Commission and Office of Production Management, May 1940 to December 1941, 1-42, 50-60 (1946); Charles M. Wiltse, Aircraft Production Under the War Production Board and Predecessor Agencies, May 1940 to April 1944 1-13 (1944) (unpublished manuscript available at the National Archives).

was new, the problem of forecasting production costs was almost as much a problem of guessing—and very rough guessing—as in the case of the costs of the experimental planes. So, with scant cost data, and dealing with the fixed price type of contract, the manufacturer and the military would simply have to negotiate, as quickly as possible, some kind of price with the hope that it would be fair.

The government was afforded a considerable measure of protection by the provisions of the Vinson-Trammell Act, 48 STAT. 505 (1934), as amended, 34 U.S.C. § 496 (1946), which was made applicable to aircraft contracts in 1939. 53 STAT. 560 (1939), 10 U.S.C. § 311 (1946). This Act required that the contractor pay back to the government any profits made by it which exceeded a stated percentage. Although the Vinson-Trammell Act was suspended with respect to army aircraft by the excess profits tax law in late 1940, 54 STAT. 1003 (1940), 34 U.S.C. § 496a (1946), Congress adopted another form of profit limitation in the Renegotiation Act of 1942. 56 STAT. 245 (1942), as amended, 50 U.S.C. App. § 1191 (1946). This Act gave the Secretary of War (in the case of War Department contracts), through his designated agencies, the power to review a manufacturer's profits under a contract and, when they were deemed too high, to reduce the contract price or fee and to require refunds to the government.

In 1940, as the tempo of war quickened, Congress authorized procurement of army aircraft by cost-plus-fixed-fee contracts, hereinafter referred to as CPFF contracts. 54 STAT. 712 (1940), 50 U.S.C. App. § 1171 (1946).[7] This form of contract was designed to avoid

[7] In addition, this statute prohibited use of the cost-plus-percentage-of-cost system of contracting.

both the evils inherent in a cost-plus-a-percentage-of-cost system of contracting and the obvious awkwardness of the fixed price contract, especially where cost forecasting was virtually impossible and there was no time to engage in refined cost analysis.[8]

With the CPFF type of contract the manufacturer made a very generalized cost estimate.[9] The fixed fee

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[8] James V. Forrestal, *Hearings Before a Subcommittee of the Senate Committee on Military Affairs on S. J. Res. 80*, 78th Cong., 2d Sess. 656, 707 (1944); Donald M. Nelson, *id.* at 608-09; Robert P. Patterson, *id.* at 666-70; ANDREW JOHN KRESS, CONTRACT PRICING—PRINCIPAL DEVELOPMENTS, STUDY OF EXPERIENCE IN INDUSTRIAL MOBILIZATION IN WORLD WAR II 27 (1946); 1 ASF, PURCHASING POLICIES AND PRACTICES 231-33; JOHN PERRY MILLER, PRICING OF MILITARY PROCUREMENTS 93, 128 (1949); THOMAS BLANCHARD WORSLEY, WARTIME ECONOMIC STABILIZATION AND THE EFFICIENCY OF GOVERNMENT PROCUREMENT 52, 236, 238-39 (1948); Welch, *Types of Defense Contracts*, 12 FED. B. J. 233, 235 (1952).

[9] Admiral Moreell characterized the process of making cost estimates as a "stab in the dark," *Hearing Before the Senate Committee on Naval Affairs Relative to Cost-Plus-Fixed-Fee Contracts*, 77th Cong., 1st Sess. 4 (1941), and subsequently pointed out at page 14 that actual costs varied considerably from original estimates. E. W. Bell, Chief of the Audit Division of the GAO, pointed out that manufacturers' cost estimates were "in some cases . . . very high and in some cases low, and in some cases . . . a mere guess." *Hearings before a Subcommittee of the Senate Committee on Military Affairs on S. J. Res. 80*, 78th Cong., 2d Sess. 633 (1944). In a lecture on *Flexible Pricing in Fixed Price Contracts* presented at the AAF Contracting Officers School, Wright Field, Dayton, Ohio, in 1944 (available at the Army Library), Major Lloyd W. Dinkelspiel pointed out (pp. 1-6) that conditions prevalent in the aircraft industry during the war made it impossible for manufacturers to make cost estimates that were more exact than guesses. See also ANDREW JOHN KRESS, CONTRACT PRICING—PRINCIPAL DEVELOPMENTS, STUDY OF EXPERIENCE IN INDUSTRIAL MOBILIZATION IN WORLD WAR II, 93, 95

was then determined as a percentage of the estimated cost, and it remained so fixed, subject to the Renegotiation Act, regardless of what the actual costs turned out to be. The contracts also provided, without any reference to the cost estimates, that the government would reimburse the manufacturer for his actual costs. Instead of spelling out cost standards in the contract, it was provided that the costs would be determined by the War Department's Contracting Officer in accordance with some previously formulated cost code, specified by reference in the contract; one of the codes most frequently adopted was Section 26.9 of Treasury Decision 5000. (R. 78)

T.D. 5000, 1940-2 CUM. BULL. 397, was adopted in August 1940 pursuant to the Vinson-Trammell Act, as amended, as the standard to be followed by the War and Navy Departments in determining costs under aviation and ship building contracts. In substance, it provided that recognized cost accounting principles should be applied in cost ascertainment.

The CPFF contracts used by the Army Air Forces were prepared by its Legal Branch from standardized provisions prescribed or authorized by the War Department; deviation from standard clauses was permissible only in exceptional cases, and then only with the approval of the chief of the AAF supply service.[10]

(1946); JOHN PERRY MILLER, PRICING OF MILITARY PROCUREMENTS 132 (1949); THOMAS BLANCHARD WORSLEY, WARTIME ECONOMIC STABILIZATION AND THE EFFICIENCY OF GOVERNMENT PROCUREMENT 237-38 (1948); Fain and Watt, *War Procurement—A New Pattern in Contracts*, 44 COL. L. REV. 127, 143-44 (1944).

[10] General Swatland, *The Procurement Functions of the AAF, the ATSC and the Contracting Officer* 9 (1944) (lecture presented at AAF Contracting Officers School, Wright Field, Dayton, Ohio, on file at Army Library); Lt. Col. James G. Scarff,

After their authorization CPFF contracts gradually came into general use and use of the fixed price contract was sharply curtailed in aircraft procurement.[11]

The principal virtues of the CPFF form were these: A premium was not placed on increased costs, as in the discredited cost-plus form, since the fee was a fixed sum of money. Elaborate negotiations over cost problems were unnecessary since the matter was left to a Contracting Officer's determination in accordance with the accepted cost accounting principles detailed in standards such as T.D. 5000. And the fixing of a single over-all price to cover elements often unknown, and

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Negotiation and Administration of Contracts 16-17 (1944) (lecture presented at AAF Contracting Officers School, Wright Field, Dayton, Ohio, on file at Army Library). See also, War Department Procurement Regulations, 7 FED. REG. 6098, §§ 81.303(a), 81.304, 81.306 (Aug. 7, 1942); 7 FED. REG. 8082, §§ 81.303(a), 81.304, 81.306 (Oct. 13, 1942). The CPFF contracts in the present case disclose on their face that they were in the regular CPFF form. The contracts are Exhibits I, J. K and L to the Stipulation of Parties, Plaintiff's Exhibit 1 in the certified record. Government war contracts are said to be "merely non-consensual, in that the standard provisions and procedures are prescribed by the government for all who wish to deal with it." Fain and Watt, *War Procurement—A New Pattern in Contracts*, 44 COL. L. REV. 127, 207 (1944).

[11] In 1944 the AAF used the CPFF contract for 70 percent of all airframe purchases, 50 percent of all engine purchases, and 40 percent of all propeller purchases. Lt. Col. James G. Scarff, *Negotiation and Administration of Contracts* 7 (1944) (lecture presented at AAF Contracting Officers School, Wright Field, Dayton, Ohio, on file at the Army Library). Between June, 1940, and December, 1943, 55 percent of all AAF purchases of ten million dollars or more were by CPFF contract. *Hearings Before a Subcommittee of the Senate Committee on Military Affairs on S. J. Res. 80*, 78th Cong., 2d Sess. 618 (1944).

rarely known with any precision, was avoided.[12] While there was the risk that cost efficiencies might not be encouraged, since they would not increase profit, experience with the CPFF form apparently was reasonably satisfactory, for a similar form is still used in military procurement.[13]

Between mid-1936 and late 1938, the respondent entered into four fixed price contracts, three with the War Department and one with the Navy Department, for the development of a new type aircraft. Three of these contracts called for construction of single "X" aircraft; one called for construction of thirteen "Y" aircraft of one of the "X" models. (R. 67) From this experimental work there grew the Airacobra, designated P-39 and later P-63.

The fixed price for these aircraft of course fell far short of actual costs. (R. 69) The excess cost to the end of 1937 of the first of the "X" craft was charged off to current profit and loss by the respondent in 1937, and those costs drop out of this case. (R. 69) But as expenditures for experimental work by this small company increased in 1938, and with the prospect that the experimental work would prove successful, capitalization of these "e and d" costs was indicated; obviously they were being incurred in order to make future production possible. Such capitalization began as of the year end of 1938 and continued until the experimental work was completed; these costs were fully set up on the books at the year end 1940. (R. 69)

There is here no dispute as to the propriety or the amount of these costs. (R. 90) They were audited by the

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[12] THEODORE W. GRASKE, THE LAW OF GOVERNMENT DEFENSE CONTRACTS § 64 (1941).

[13] 62 STAT. 21 (1948), 41 U.S.C. §§ 151 *et seq.* (Supp. V 1952).

War Department and the respondent's figures were revised in accordance with this audit. (R. 73) Nor is there here any dispute that these costs were incurred in the development of designs, devices, and principles used in the planes ultimately put into production and are properly to be amortized as costs of such craft. (R. 95-99)

Beginning in 1939 and running into 1941 the respondent entered into a series of fixed price contracts with the War Department and with the British for the production of the P-39. There were seven such contracts, the last one being entered into with the War Department on June 5, 1941. (R. 71)

When production was undertaken, the respondent had to build "production tools" in a substantial amount. As we have seen, at that point it would be necessary to set up assembly lines, with a maze of devices especially designed for the P-39. (R. 72) The cost of these "production tools" was also deferred by the respondent in the same way as the "e and d" costs, to be amortized to future production; these costs were incurred month by month from April, 1939, through December, 1940, by which time they were fully set up on the books. (R. 73, 76; see Plaintiff's Exhibit 12 in the certified record.)

Like the "e and d" costs, there is here no dispute as to the amount or the propriety of these production tooling costs. (R. 90) They were audited by the War Department and the respondent's figures were revised accordingly. (R. 73) Nor is there here any dispute that the production tools were necessary for and were used in the production of the P-39 and that the original cost thereof is properly to be amortized instead of being currently expensed. (R. 99-100)

The total deferred "e and d" costs subject to amortization were $1,499,739.23; the total production tooling cost subject to amortization was $1,874,725.77. (R. 73)

The respondent's amortization was based on this plan: The total amount to be amortized as of the beginning of a calendar year would be divided by the sum of the P-39's on order at that time and the additional P-39's ordered in the course of the year; this would give, at the year end, the amount to be assigned to the cost of each aircraft. The respondent would then charge off, at the year's end, an amount arrived at by multiplying the number of P-39's actually delivered during the year by the amount thus assigned to the cost of each aircraft. (R. 73-74, 84) There has never been any dispute that this was a reasonable and proper basis for amortization. (R. 90)

The respondent's last fixed price type of contract was entered into in June, 1941. (R. 71) The next P-39 order was two months later, on August 14, 1941, and the contract therefor was in the then comparatively new CPFF form. Thereafter all of respondent's contracts were CPFF. (R. 77) There were five such. The second was entered into in September, 1941, the third in June, 1942, the fourth on September 28, 1943, and the fifth in January, 1944.[14]

Of course, under the amortization plan which the respondent had been following, the deferred costs would have been assigned in ordinary course to the

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[14] The fifth contract was for the P-63, a development from the P-39. This contract was later combined with the third contract which had been changed to call for P-63's. (R. 77) The lower Court treated the case as involving four CPFF contracts, in view of this combination; the War Department Board of Contract Appeals treated the case as involving five contracts. (R. 92)

craft produced under the CPFF contracts as well as to those produced under the fixed price contracts. But this did not happen. As found by the Court below:

> "According to the plan of amortization above referred to, a portion of the deferred experimental, development and production tooling costs would have been allocated to planes produced and delivered under these CPFF contracts. However, plaintiff's officials had been advised by Army Air Force officials that the deferred expenses in question might not be approved for reimbursement under CPFF contracts being negotiated. In order to avoid any question of allowable reimbursements, plaintiff changed its original plan of amortization by limiting the allocation of the deferred charges to its fixed-price production contracts only." (R. 74)

On this basis, the full amortization was accrued on the respondent's books by the year end of 1942, by which time all of the craft produced under the fixed price contracts had been delivered. (R. 76)

In 1942, however, the Bureau of Internal Revenue questioned the respondent's failure to amortize over all the P-39 aircraft. (R. 81) It insisted that this resulted in an understatement of taxable net income for 1941 by assigning to the P-39's delivered under fixed price contracts for that year a disproportionate amount of costs; the Bureau took the same position with respect to the respondent's income for the year 1942. (R. 82) Assignment of the costs to the P-39's produced under the CPFF contracts as well as those under the fixed price contracts would decrease the respondent's expenses for the years 1941 and 1942 and would mean an

additional normal and excess profits tax for those years amounting to $1,337,474.89. This additional amount was in fact assessed by the Bureau and paid by the respondent. (R. 82)

In the meantime the War Department had taken up the question of renegotiation with the respondent. (R. 82) Under the authority of the Secretary of War, pursuant to the Renegotiation Act, a Price Adjustment Section had the power to revise the price of a contract in the light of various statutory standards, including costs of performance, subject to review by a Price Adjustment Board in the War Department. The Chief of the Price Adjustment Section concerned with the respondent, Major Phagan, took exactly the same position as had the Bureau of Internal Revenue with respect to the amortization of the respondent's deferred costs over all P-39's. (R. 106) Accordingly the respondent, early in September, 1943, addressed a letter to Major Phagan agreeing to amortize the costs over all the aircraft instead of limiting amortization only to those produced under fixed price contracts, provided that the amounts "disallowed by you against fixed price contracts become items of reimbursable costs under" the CPFF contracts. (R. 82-84) On September 9, 1943, Major Phagan approved this course by the respondent. (R. 84)

The respondent restored to a deferred account on its books the sum of $2,286,819.55, representing the amount attributable to aircraft under CPFF contracts. (R. 84) There is no dispute in this case as to the propriety of this amount or the basis on which it was determined. (R. 90)

In August, 1943, the respondent had submitted to the War Department Contracting Officer administering its CPFF contracts cost vouchers providing for

reimbursement of the portion of this restored deferred account attributable to P-39's delivered under CPFF contracts through August, 1943.[15] This sum amounted to $1,299,856.02. (R. 85)

The War Department's Assistant Resident Auditor, assigned to the respondent, recommended that these vouchers not be paid. The Resident Auditor disagreed and recommended their approval. The Contracting Officer did approve them for reimbursement under the CPFF contracts, and the respondent was paid that sum by the War Department's Finance Officer in September, 1943. (R. 85)[15a]

Beginning in October, 1943, the respondent submitted additional vouchers for the remainder of the costs in the deferred account, applicable to aircraft delivered subsequent to August, 1943. These vouchers totaled $986,963.93. (R. 85) At about the time these vouchers began to arrive for audit the Resident Auditor and Contracting Officer were both replaced. The Assistant Resident Auditor again recommended against approval of vouchers covering these costs. (R. 86) The new Resident Auditor in December, 1943, requested advice from the Air Technical Service Command as to treatment of these costs, and the matter was held in abeyance for over a year until, after receiving

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[15] See Stipulation of Parties, Plaintiff's Exhibit 1, pp. 16-17, in the certified record.

[15a] The function of the Auditors was to assist and advise the Contracting Officer. ARMY TM 14-1000, ADMINISTRATIVE AUDIT PROCEDURES FOR COST-PLUS-A-FIXED-FEE SUPPLY CONTRACTS ¶¶ 5-6 (1944); Major Richard H. Demuth, *Administration of CPFF Contracts* 5-6 (1944) (lecture presented at AAF Contracting Officers School, Wright Field, Dayton, Ohio, on file at Army Library). The function of the Finance Officer was to make payments according to the Contracting Officer's order. ARMY REGS. 35-180 ¶3 (May 27, 1942).

such advice, the new Contracting Officer declined approval of the additional vouchers in January and March, 1945. *Infra*, at pp. 16-17. (R. 88-89)[16]

Meanwhile, in February, 1944, the Resident Auditor was again replaced. In April and May of 1944 the General Accounting Office submitted to this third Resident Auditor informal exceptions to the payment of $1,299,856.02 made to the respondent in September, 1943. (R. 86-87) In June, 1944, the Resident Auditor advised the General Accounting Office that deductions in that amount would be made from other vouchers of the respondent which were pending. (R. 87) The Contracting Officer, however, held up the vouchers from which deductions had been made by the Resident Auditor and took no action thereon until September, 1944. (R. 87) Prior to that time, on August 18, 1944, the Comptroller General had issued formal notices of exception and suspended the accounts of the War Department's Finance Officer who had made the payment to the respondent. (R. 87) At first there were two such exceptions which for some unexplained reason failed to include approximately $125,000 of the previous payment to the respondent. The Finance Officer immediately recouped the amounts in question by deducting these sums from vouchers otherwise due the respondent; the Comptroller General was notified thereof on August 25, 1944, four days after the excep-

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[16] Each of the two sets of vouchers covered both "e and d" costs and production tooling costs as follows (R. 85, 88):

	Total	"E and d" Costs	Production Tooling Costs
First set	$1,299,856.02	$ 407,871.26	$ 891,984.76
Second set	986,963.93	628,047.47	358,916.46
	$2,286,819.95	$1,035,918.73	$1,250,901.22

tions were received. (R. 87) Early in September the Contracting Officer transmitted to the Finance Officer for settlement groups of the respondent's vouchers, including those from which the Resident Auditor had made deductions in June. (R. 87) At the time of transmitting these vouchers the Contracting Officer restored the deductions, except for deduction of the $125,000 which had not been recouped by the Finance Officer and which had been overlooked in the Comptroller General's formal exceptions. (R. 87) At almost the same time the Finance Officer received from the Comptroller General a formal exception and suspension of his accounts with respect to this $125,000, and the Finance Officer immediately advised the Comptroller General that this sum had also been recouped by deduction from vouchers for sums otherwise due the respondent. (R. 88)

This recoupment at the instance of the Comptroller General was completed by September, 1944. (R. 88) It is important to note that the Contracting Officer took no action whatsoever with respect to this recoupment except for the sum of $125,000, and that *both his action and the action of the Finance Officer were merely in response to the Comptroller General's exceptions and did not purport to rule on any issue of cost reimbursability.*

In a memorandum dated November 13, 1944, the Chief of Procurement of the Air Technical Service Command finally responded to the December, 1943, request of the then Resident Auditor for advice as to treatment of these costs. (R. 88) On January 10, 1945, the second Contracting Officer transmitted to the respondent his decision on the vouchers for the sum of $986,963.93—the sum allocated to deliveries after August, 1943, to which we referred *supra* at p. 14. This

decision, in writing, opened with the following statement:

> "1. Forwarded herewith is a copy of a decision made by the Chief of the Procurement Division of the Air Technical Service Command on the reimbursement of amortization of development and experimental expense over CPFF contracts.
>
> "2. This office incorporates the decision of the Chief of the Procurement Division as a finding of facts in denying reimbursement to the contractor for this expenditure, as requested on Audit Bureau Vouchers, as follows:"

There were then listed the series of vouchers which totaled $986,963.93. Attached to this decision was a copy of the memorandum of November 13, 1944, from the Chief of Procurement. This memorandum discussed the question of allocating the deferred costs to aircraft produced under CPFF contracts, without any distinction between the sums which had already been paid and the sums remaining on the pending vouchers, referred to the original informal exceptions of the General Accounting Office, briefly discussed the merits of the question, and concluded that, "It is therefore the opinion of this Headquarters" that the respondent is not entitled to reimbursement under its CPFF contracts "for any portion of the" deferred costs. (R. 88-89)

Under date of March 1, 1945, the same Contracting Officer sent to the respondent a further communication rescinding his January action and forwarding a new decision. (R. 89) The new decision listed the same unpaid vouchers as had the previous one (*i.e.*,

those totaling $986,963.93). It then proceeded to copy almost word for word the communication from the Chief of Procurement, a copy of which had been sent to the respondent in January, except that it omitted an introductory paragraph and substituted the words, "It is, therefore, the decision of the Contracting Officer", in the concluding sentence for the words, "It is therefore the opinion of this Headquarters". (R. 89)[17]

At this point the respondent made timely appeal to the War Department Board of Contract Appeals from the Contracting Officer's decision. (R. 89) Since the only action of the Contracting Officer was the disapproval of the vouchers for $986,963.93, the appeal was regarded as an appeal from that action. (R. 89) However, the Board discussed the issues in terms which would be equally applicable to the question of reimbursability of the $1,299,856.02, approved by the first Contracting Officer, had the Board believed it was acting upon that item. (R. 89-92)

The Board held that, "Under the circumstances here present, the Board is of the opinion that the costs are not reimbursable under the subject contracts." (R. 91-92)

Thereafter the respondent filed this suit in the Court below.

A disputes clause in each of the contracts provides that disputes concerning questions of fact shall be decided by the Contracting Officer, subject to appeal to the Secretary of War or his designated representa-

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[17] The Contracting Officer's decision of January 10, with attached memorandum from the Chief of Procurement, Plaintiff's Exhibit 25 in the certified record, and his communication and decision of March 1, 1945, Plaintiff's Exhibit 26 in the certified record, are printed in full in Appendix C.

tives.[17a] Three contracts authorized the Board of Contract Appeals to act as the designated representative of the Secretary of War; one contract provided only for appeal to the individual designated as representative of the Secretary of War, in this case the President of the Board. In both instances it was provided by a memorandum of the Secretary of War dated July 4, 1944, 10 CODE FED. REGS. § 803.318d (g) (Supp. 1944), that the designated representatives could consider questions of law.[18] There is no contention here that the Board's determinations of such questions have any finality; the petitioner's Petition for Certiorari states (at p. 10), "There is no doubt that the 'Disputes' provisions in Article 16 of each of the CPFF contracts made final and conclusive only those administrative determinations concerning questions of fact."

While the Court below made much more extensive findings than did the War Department Board, there is no significant difference between the findings except in the legal conclusions as to the interpretation of the contracts.

The contracts, as we have noted, do not define reimbursable costs save by incorporating, by reference, the provisions of T. D. 5000. The Board, recognizing that the developments resulting from the "e and d" expenditures were incorporated in all P-39's and that the production tooling was used in their manufacture under the CPFF contracts, held that the costs here in

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[17a] The disputes clauses in respondent's CPFF contracts were in two forms. Both are printed in Appendix B, pp. 84-88.

[18] The Board recognized in its opinion in this case that it was acting pursuant to such memorandum when it said, "Insofar as the questions presented by this appeal are questions of law they will be administratively determined pursuant to the memorandum of Secretary of War dated 4 July 1944." (R. 90)

question would be embraced by T. D. 5000 had it not been that:

(a) They were incurred prior to entering into these contracts and would have been incurred regardless of whether these contracts had been entered into. (R. 91)

(b) The respondent was charging these costs off to the fixed price contracts when it negotiated the CPFF contracts and at that time had no intention "of seeking reimbursement for such costs". (R. 91)

The Court, on the other hand, held that it was immaterial, under the terms of T.D. 5000, that what amounted to capital costs were incurred before any CPFF contracts were entered into or were occasioned by work which, at the time, was called for by fixed price contracts; that the experimental costs were incurred in expectation of production and the production under the CPFF contracts "represented a portion of the fulfillment of that expectation"; and that the production tooling was actually used not only for production under the fixed price contracts but also for production of exactly the same aircraft under the CPFF contracts. (R. 125-26) As to the respondent's intention "not to request reimbursement", the Court held that no such understanding was expressed in the contracts and that therefore the respondent's original intention did not create an immunity on the part of the petitioner. (R. 126-28)

The petitioner also argued to the lower Court that the respondent's appeal to the Board was directed only to the vouchers for $986,963.93 and that therefore the respondent had failed to exhaust its contractual

remedies with respect to the claim for $1,299,856.02 and so was foreclosed from recovering that sum. The Court rejected this argument. See *infra* p. 56 *et seq.*

While this matter was pending before the War Department Board the respondent's renegotiation agreement for the fiscal year 1942 was executed. It provided for a refund to the petitioner of $7,714,000, after tax credits. (R. 93) It also recognized that the respondent had adjusted its amortization of the deferred costs as required by the Bureau of Internal Revenue (R. 94) and provided that if the costs here in question are reimbursed under the CPFF contracts (as contemplated in the agreement of September, 1943, with the Chief of the Price Adjustment Section, *supra* at p. 13), there shall be a further refund to the petitioner of $667,000 with appropriate tax credit. (R. 94) Thus, if the lower Court is sustained, the respondent's cost reimbursement, renegotiation, and tax relationships with the petitioner will be on the same basis.

QUESTIONS PRESENTED

1. Under a standard CPFF contract, providing for cost reimbursement in accordance with the standards of T. D. 5000, should reimbursement be denied, for items coming within those standards, because the contractor did not originally expect to request reimbursement?

2. Is the question just stated a question of fact on which decision under the fact disputes clause of CPFF contracts is final, or is it a question of law open to judicial determination?

3. Is a contractor foreclosed from bringing suit on a portion of a claim because a Board of Contract Appeals regarded the contractor's appeal as not in-

volving such portion, despite the fact that the contractor did appeal from the only adverse decision of the Contracting Officer?

4. Is a decision of the Contracting Officer, made with knowledge of the relevant facts, approving reimbursement of a cost under the cost reimbursement provision of a standard CPFF contract open to reexamination either by successor Officers or in court?

Our discussion of the questions will be in the order stated above; the discussion of the last two questions will be combined.

SUMMARY OF ARGUMENT

I

The CPFF contracts in this suit provide that allowable costs will be determined by the Contracting Officer in accordance with T.D. 5000. The experimental work, allocated costs of which are involved in this case, developed the aircraft produced under those contracts. And the production tooling, allocated costs of which are also involved, was necessary for and was used in such production. T.D. 5000, as interpreted both by the War Department Board and by the lower Court, provides that such costs are allowable.

The Board held, however, that in this case such costs are not to be reimbursed because the respondent, when it negotiated the contracts, did not expect to seek reimbursement and consequently did not amortize such costs, on its books, over the production under such contracts during the first two years of such production. The lower Court held that the contract obligation is to be determined by the contracts as written, and not by some previous unilateral expectation or intent of one of the parties. The Court was correct.

CPFF contracts, framed by the petitioner itself, clearly provide that costs defined in T.D. 5000 shall be reimbursed. Even had there been an understanding between the parties that the costs in question would not be reimbursed, that understanding could not be enforced unless expressed in the written contracts; and here the findings show that there was not even such an understanding.

The petitioner's argument that T.D. 5000 merely defines the costs which *may* be approved by the Contracting Officer if he deems the "facts and circumstances" to warrant approval cannot be accepted. Such an argument would make of the contracts nothing but the definition of a *privilege* on the part of the petitioner to pay the respondent. But the contracts expressly state an *obligation* to pay.

II

The contracts provide that disputes concerning questions of fact shall be finally decided by a specified process within the War Department. The petitioner argues that the decision of the War Department Board was final under that provision.

The petitioner is incorrect in its statement that the question presented is whether the costs here involved were necessary or incident to the performance of the contracts. The only question is whether costs defined in T.D. 5000 are not to be reimbursed solely because the respondent did not at first expect to request reimbursement. The answer to this question turns wholly upon interpretation of the contracts. That is a matter of law open to judicial determination and not concluded by Departmental process. Fact disputes clauses such as those included in these contracts have

always been regarded as leaving to the courts the final decision of questions of contract interpretation. This view should not now be overturned.

III

A first set of vouchers, covering part of the costs involved here, was approved by the Contracting Officer and payment thereon was made to the respondent by the petitioner. Thereafter this payment was recouped at the instance of the Comptroller General, a stranger to the contracts, who filed exceptions and suspended the accounts of the Finance Officer who had made the payment. Still later a new Contracting Officer decided that a second set of vouchers, covering the remainder of the costs involved here, should be disapproved. This decision referred generally to the whole claim of the respondent, but the only matter pending before such Officer was the second set of vouchers and the only action taken by him, therefore, was disapproval of that set of vouchers. This decision was appealed in accordance with the Departmental process provided for in the contracts; on appeal the question was treated as involving only the second set of vouchers, although the findings and decision on appeal would have been equally applicable to the first set of vouchers if they had been deemed to be involved in the appeal. The petitioner now urges that contractual remedies were not exhausted before this suit was filed, with respect to the claim based on the first set of vouchers, because the appeal dealt only with the second set of vouchers; at the same time the petitioner insists that the second Contracting Officer's decision actually dealt with the whole claim.

This technical defense was unanimously rejected by the lower Court and properly so. It is enough to say

that the appeal was from the decision of the second Contracting Officer, whatever that decision was.

Furthermore, the contracts provide that the petitioner will currently reimburse the respondent for costs approved by the Contracting Officer. The first Contracting Officer did approve the first set of vouchers. There is no provision for redetermination of such an approval by a successor Contracting Officer, and it is contrary to the contractual scheme to read such a provision into the contracts. Nor can the petitioner repudiate the decision of the first Contracting Officer when suit is brought to recover on the cost vouchers approved by him. The contracts, written by the petitioner itself, vest in the petitioner's own Officer the power to determine, and such determination must have been intended to bind the petitioner. Hence the respondent was not called upon to appeal an adverse decision of a successor Officer upon vouchers previously approved by his predecessor, even if that decision purported to deal with such vouchers. The respondent is entitled to payment of the first set of vouchers merely upon proof of the first Officer's approval thereof, at least in the absence of fraud or misapprehension of the facts on the part of the first Officer when he took his action.

Alternatively, the proper interpretation of the contracts is that the decision of its own Officer will bind the petitioner on questions of fact, so that if the petitioner is correct in its argument that a question of fact is involved here the decision of the first Contracting Officer on the first set of vouchers is conclusive.

It will be recognized, of course, that if the question here is one of law, as we argue in our point II, the defense of failure to exhaust contractual remedies is not applicable, for the contracts do not purport to provide a process for the determination of such a question.

ARGUMENT

I

The Charges for Experimental and Development and Production Tooling Costs Made to the CPFF Contracts were Reimbursable Costs Under the Provisions of those Contracts.

Petitioner's argument as to the reimbursability of the costs here involved, and as to whether reimbursability is a question of fact or law, is based throughout on an inaccurate statement of what the issue really is. The issue is not, as petitioner asserts in its argument, whether the costs were "incurred as a necessary incident to the performance of the CPFF contracts." (Brief, p. 18) The question is whether costs otherwise admittedly covered by the cost reimbursement provisions of the contracts must nevertheless be denied reimbursement because at the time the contracts were negotiated respondent did not expect to seek reimbursement. When the question is so stated, and the provisions of the contracts are analyzed, it becomes apparent that the lower Court correctly interpreted the CPFF contracts to require reimbursement, and that its decision was one of a question of law open to its determination.

A. THE EXPERIMENTAL AND DEVELOPMENT AND PRODUCTION TOOLING COSTS ARE ALLOWABLE COSTS UNDER T. D. 5000.

Each of the CPFF contracts provides in Article 3(b) that:

> ". . . allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated . . . in Section 26.9 of . . . T.D. 5000 . . ." (R. 78)

Petitioner's brief does not analyze the provisions of T.D. 5000 or discuss the facts which led the War Department Board and the lower Court to conclude that the costs here in question were within its terms. Conceding that the costs are within T.D. 5000, petitioner argues that the issue still remains whether the costs were incurred as a necessary incident of performance of the contracts, and that certain facts show that they were not. Both the terms of T.D. 5000 and the findings below are of vital importance.

The provisions of T.D. 5000 with respect to cost reimbursement are printed in full in Appendix A, pp. 73-83. The provisions immediately relevant to this controversy are as follows:

> "(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract; and (2) the proper proportion of any indirect costs . . . incident to and necessary for the performance of the contract or subcontract.
>
> * * * * *
>
> "(e) *Factory cost.* . . .
>
> "(5) *Indirect factory expenses.*—Items, usually termed 'factory overhead,' which are not directly chargeable to the factory cost of performing the contract or subcontract but which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:
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> * * * * *

> "(D) *Fixed charges and obsolescence.*—Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as . . . allowances for depreciation of such property, . . .
>
> "(d) *Other manufacturing cost.*—Other manufacturing cost . . . includes items of manufacturing costs which are not properly or satisfactorily chargeable to factory costs . . . but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, . . . 'deferred' or 'unliquidated' experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. . . ."

In considering the reimbursability of these costs the War Department Board *made absolutely no finding that they were not incident to or necessary for the performance* of the CPFF contracts.

First the Board found that:

> "There is no dispute between the parties as to the amount of the costs or as to the propriety of the method of allocation used by [respondent]." (R. 90)

Then, as to the "e and d" costs, it found that:

> "The experimental and development costs are clearly within the category of indirect costs as defined by T.D. 5000 and are specifically covered by Section 26.9(d) of T.D. 5000—set out above." (R. 90)

As to the production tooling costs, the Board found that:

> "There is no specific reference in T.D. 5000 to the amortization of production tooling costs and appellant has not pointed out a specific provision of T.D. 5000 which it considers as providing for the allowance of such an item of cost. In the pamphlet issued by the War and Navy Departments entitled 'Explanation of Principles for Determination of Costs Under Government Contracts' (Par. 18), it is indicated that items such as royalties and the amortization of the initial cost of dies, patterns, and special tools can logically be classified as direct shop costs and be charged to contracts on an equitable basis of apportionment. Section 26.9(e)(5)(D) of T.D. 5000 set out above also provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. It is clear from the record and evidence that the production tooling was used in the performance of CPFF contracts calling for the production of the P-39 type of airplane. It would seem, therefore, that items of this type are within the intent and meaning of T.D. 5000." (R. 90)

With respect to the production tooling the Board thus specifically found that it was used in performance of

the contracts and therefore that its cost was within the intent and meaning of T.D. 5000. The finding that experimental and development costs were covered by T.D. 5000 is plainly based on a recognition that the experimental work developed the Airacobra produced under the CPFF contracts.

The Court of Claims also made specific findings as to the use in performing the CPFF contracts of both the production tooling (R. 99-100) and the results of the experimental and development work (R. 95-99). As the Court said, "... had the experiments not been conducted and the charges not incurred, defendant [*i.e.*, petitioner] could not have secured any of the planes from plaintiff [*i.e.*, respondent]." (R. 130) There can be no doubt of the correctness of these findings.

The experimental work represented a brilliant pioneering development of distinctive features which made the Airacobra a unique and advanced plane of its day.

As to the production tooling, P-39's could not be produced without it. As a matter of fact when P-39 production ceased the tooling had to be scrapped and the petitioner was credited with its salvage value under the CPFF contracts. (R. 99, 124) And when the production under the CPFF contracts began there were devoted to it production tools which were the equivalent of new tools (R. 99)—for after their original construction, as tooling wore out or became obsolete while production under the fixed price contracts proceeded, the cost of replacing and reworking such tools had not been deferred but had been charged against current production (R. 73) so that the continued production under the CPFF contracts had the benefit of a set of

tools completely in repair and up to date. (R. 99, 124)[19]

If the production under the fixed price contracts and that under the CPFF contracts had been physically separated in point of time, with the former completed before the latter began, this would have been the situation: The respondent could have scrapped the production tools upon the completion of the fixed price contracts and pocketed the salvage value thereof. Then it could have built a new set of tools for the CPFF production and there would be no question whatever but that the entire cost thereof should be amortized over the CPFF contracts. Needless to say, the petitioner would have paid a large amount therefor. As it was, in this case before CPFF production began the respondent continuously maintained and replaced the tools, treating the cost of maintenance and replacement as current cost of fixed price production, though the maintained and replaced tools were later devoted to CPFF production; and the CPFF production got the full credit for the *entire* salvage value of the tools at the conclusion of the CPFF production. (R. 99) It is small wonder that the lower Court found that T.D. 5000 contemplated that CPFF production should be charged with a fair portion of the original cost of the tools.

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[19] As the lower Court found, ". . . when the work was started on the CPFF contracts, the value of the original tooling was substantially the same as its original cost" in view of its constant repair and replacement theretofore. (R. 124)

B. THE FACTS RELIED ON BY PETITIONER AS A BASIS FOR DENYING REIMBURSEMENT HAVE SIGNIFICANCE ONLY IN TERMS OF RESPONDENT'S ORIGINAL INTENTION OR EXPECTATION WITH RESPECT TO REIMBURSEMENT.

The War Department Board stated, however, that, while the costs were covered by T.D. 5000, it did not follow that such costs must be reimbursed in all cases and under all circumstances. (R. 90) It then found certain facts which it considered to be pertinent. (R. 91) These same facts are now relied on by the petitioner. Analysis discloses that these facts have significance only in terms of the original expectation, purpose or intention of respondent as to whether it would request reimbursement of these costs.

These facts fall into two general categories.

The first relates to the time of the expenditures: They were made prior to the CPFF contracts and would have been made whether or not there had been any CPFF contracts. Save as these facts enlighten the respondent's state of mind when the CPFF contracts were negotiated, they obviously can have no legal significance. Typically costs of this type are incurred in advance; and typically, where production is to occur over a period of time under a series of orders or contracts, all prospective orders will not be in hand when the costs are incurred. *Douglas Aircraft Co.* v. *United States*, 95 Ct. Cl. 140 (1941).

The Board's reference to the facts concerning the time when the costs were incurred was simply an introduction to the second category of facts relied on by it, namely facts showing that at the time the CPFF contracts were negotiated the respondent did not intend to request reimbursement of these costs under the CPFF contracts.

There is no dispute as to these facts. What happened is set forth by the lower Court:

> ". . . it has not been shown that defendant relied on plaintiff's intention not to request reimbursement and because of such reliance changed its position so as to work an estoppel. The record merely indicates that some agent of defendant had expressed the opinion to plaintiff, prior to the execution of the CPFF contracts, that experimental, development, and production tooling expenses would not be reimbursable, and that plaintiff accordingly decided not to request reimbursement. This understanding, if any, was not expressed in the contracts ultimately entered into, although it might easily have been done by expressly excluding such items in the contract." (R. 126-27)

The War Department Board's findings are fully in accord. Indeed, that Board found that:

> ". . . no specific consideration was given to the question of reimbursement [of these costs] in the negotiation of the subject contracts." (R. 91)

Thus there is not the remotest suggestion that the reimbursement provisions of the contract were in any way affected or that the petitioner was induced to change its position by the respondent's original expectation not to seek reimbursement of these costs. Neither findings nor evidence hints at anything of the sort. The petitioner makes no such contention, and it could not do so on this record. And all that the petitioner says in its brief about the respondent's bookkeeping, certain statements by the respondent's officials, and what was included in the cost estimates merely elaborates upon the fact that, prior to the time when the Bureau of Internal Revenue forced the issue, the respond-

ent had not expected to request reimbursement of these costs.

As far as the respondent's bookkeeping is concerned, the situation is clear cut. Prior to the time the CPFF contracts were entered into, the *fact* is that the costs were being amortized over fixed price contracts with the petitioner and the British. (R. 73-76) It could not have been otherwise, *for there was no other P-39 production.* As one after another fixed price contract was secured, the planes ordered thereunder would come into the amortization base. This is evident not only from the findings (R. 73-74) but also from the statements of the respondent's accountants, Price, Waterhouse & Co., in the respondent's Annual Reports (R. 74-76) to which the petitioner's brief refers with some emphasis. Consequently if the contract of August 14, 1941, had been another fixed price form of contract instead of being the first CPFF form of contract, the respondent's bookkeeping would have embraced in the amortization the planes produced under it just as it did those produced under the last fixed price contract entered into only two months previously. (R. 74, 76)

It makes no difference how this bookkeeping is described—whether it be described as amortization over *fixed price* P-39 contracts or as amortization over *any* P-39 contracts, the *fact* is that until August 14, 1941, there were no contracts except fixed price contracts and the respondent's bookkeeping amortized only over such contracts.

Of course the amortization plan being followed by the respondent, see *supra*, p. 11, required a determination of amortization at each year end. Consequently it was not until the end of 1941 that there was any occasion for distinguishing between different

P-39's in the recording of amortization on the books. At that time the CPFF contract production was not brought into the amortization base. But all that this means is that the respondent's intention at that time not to seek reimbursement was reflected in the books which its Comptroller was keeping. And our contention, agreed to by the lower Court, is that as a matter of law that fact is irrelevant, for books do not create or pay costs but merely record them, and if books are wrong in the reflection of costs the books can be changed. PATON, ADVANCED ACCOUNTING 269 (1947); HATFIELD, SANDERS, BURTON, ACCOUNTING PRINCIPLES AND PRACTICE 311-12 (1940). Books cannot change facts. *Doyle* v. *Mitchell Bros. Co.*, 247 U.S. 179, 187 (1918); *E. P. Greenwood*, 34 B.T.A. 1209, 1214-15 (1936). *Cf. Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 643, n. 40 (1944). The cases are literally legion where costs are found to be different from their recording.[20] Except where there is some special statutory provision or some special consideration of policy, such as the strict rule of annual accounting periods for income tax purposes, accounting entries bind no one. *Norfolk & Western Ry.* v.

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[20] A taxpayer may be allowed to correct a tax return for an earlier year by taking depreciation on patents even though no depreciation was claimed thereon in the original return. Union Metal Mfg. Co., 1 B.T.A. 395 (1925). The SEC conditions the issuance and sale of securities on such retroactive accounting adjustments as the write-down of a property account. See, *e.g.*, Utah Power and Light Co., 14 S.E.C. 764, 781-82 (1943). Rate orders finding assets to have been overdepreciated have corrected such overdepreciation. See, *e.g.*, *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 596-98 (1944); *Lindheimer* v. *Illinois Bell Telephone Co.*, 292 U.S. 151, 165, 169-75 (1934).

United States, 287 U.S. 134, 141-42 (1932); *Commissioner* v. *Union Pacific R.R.*, 86 F. 2d 637, 639 (2d Cir. 1936); *New York Central R.R.* v. *Commissioner*, 79 F.2d 247 (2d Cir. 1935), *cert. denied*, 296 U.S. 653 (1935); *Bessemer Investment Co.* v. *Commissioner*, 31 F. 2d 248 (2d Cir. 1929); *Douglas Aircraft Co.* v. *United States*, 95 Ct. Cl. 140, 148 (1941); Hills, *Statement of Legal Concepts of Accounting*, 36 Iowa L. Rev. 198, 208-09, 225 (1951).[21]

The petitioner also refers to a statement made by one of the respondent's officials during the time between the letting of the first CPFF contracts and the respondent's decision to seek reimbursement. The statement is quoted by the petitioner (Brief, p. 8) but it is not identified. The petitioner neglects to explain that it is a mere intra-office memorandum of September 19, 1942, from the respondents Treasurer to its Comptroller, dealing with the argument which the respondent was then having with the Bureau of Internal

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[21] There is a suggestion in the War Department Board's opinion that respondent did not prove that the costs in question were not recovered under the fixed price contracts. (R. 91) This reflected a similar suggestion by the second Contracting Officer to the effect that profits under fixed price production were "more than enough" to recover these costs "and were so treated on the books" of the respondent. (R. 88) These suggestions point to an argument, made below, that the Government would be paying twice for these costs if the respondent prevails. Aside from the fact that the Government was not the sole fixed price customer, such a point is so clearly without merit that the petitioner does not pursue it here. The making of entries on books does not "recover" costs; still less does it pay them. Furthermore, this is not even a case where an asset, fully amortized *before* a particular production process began, is being revalued and charged off *anew* to that production. Nothing is proposed here except to charge to the CPFF contracts a proper portion of *those costs which had not yet been amortized when CPFF production began.*

Revenue and stating that the costs should be allowed as then recorded on the respondent's books because amortization thereof over the CPFF contracts would be permissible only if such costs had been "included in the original negotiations of such [CPFF] contract. No provision is made for that on any of our cost plus contracts in view of the position taken by the Government that prior to our entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses." (R. 82) Such an intra-office memorandum in September, 1942, obviously has nothing to do with the case. The respondent was arguing with the Bureau about a large deficiency assessment, and the statement by the respondent's Treasurer to its Comptroller during that argument certainly cannot define the petitioner's contractual obligation under contracts entered into both long before and long after that time. Furthermore, all that the memorandum reflects is a mistaken understanding in the mind of the Treasurer as to the law; he quite obviously had been led to believe by someone in the War Department that cost reimbursement under a CPFF contract hinged on whether the cost item was "included in the original negotiations." (R. 82) A layman might believe this; but as we shall see there is no basis for this mistaken conception.[22]

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[22] Petitioner also quotes in its brief (p. 9) two sentences from a statement of accounting policies by respondent's Comptroller in April, 1943. (R. 82) The petitioner has misconstrued the passage. Actually it says no more than that current CPFF experimental, development and production tooling expenses were charged *directly* to production, as distinguished from overhead. (Tr. 262-63) The point is immaterial, however, for it is evident that at that particular time the costs here in question had not been charged to CPFF production.

The petitioner and the War Department Board also cite the fact that the respondent did not include any allowance for these costs in the estimated cost of the CPFF contracts which it submitted to the War Department. (R. 91) The Board did not intimate that this fact was of any significance save as it may have some bearing on the respondent's original intention.

The fact is that the respondent made no such allowance in its cost estimates submitted to the War Department *either* for fixed price contracts (R. 73) *or* for the CPFF contracts. (R. 91) No one would suggest that the absence from the fixed price estimates of an allowance for these costs would mean that an appropriate portion thereof is not properly a cost of production thereunder. No more can it be suggested that their omission from estimates made in connection with the CPFF contracts means that an appropriate share thereof is not properly a cost of production thereunder.

C. RESPONDENT'S ORIGINAL INTENTION REGARDING REIMBURSEMENT OF COSTS IS IRRELEVANT.

We come now to the question of the legal significance of the respondent's original intention.

As we have seen, the respondent did not at first expect to seek reimbursement because it had been given the impression by War Department officials "that the deferred expenses in question might not be approved for reimbursement." (R. 74) CPFF contracts were then quite new, respondent had no experience with them (Tr. 212), and there were many unresolved questions concerning cost reimbursability. Indeed, there doubtless still are. This is not the first or the last time that a contractor, for any one of a dozen reasons, entered into a CPFF contract thinking that it would

not seek reimbursement of some particular cost. But this is the first time, as far as we know, that it has been suggested that such a thought should deprive a contractor of rights granted him by the contract—that the CPFF contract will not permit reimbursement unless the contractor has decided to seek reimbursement and asserts such an intention in the course of negotiations.

1. To overrule the lower court would be to disregard the underlying theory and the specific provisions of the CPFF contracts.

A consideration of the underlying theory of CPFF contracts and of the specific provisions of the contracts designed to carry out that theory makes it entirely clear that a contractor's intention with respect to seeking reimbursement of particular costs is expressly excluded from the circumstances made pertinent to the legal *right* to reimbursement. As indicated in our statement of the case, *supra,* pp. 5-9, despite its shortcomings the CPFF contract was and still is a necessary procurement device in a period when rapid expansion of facilities and prompt provision of war materials are essential, but where conditions are changing so rapidly and the materials to be produced are so complicated and subject to such continual variances that any detailed determination of costs in advance is impracticable. The whole purpose of the CPFF contract is to leave cost determinations to the application of the standards of T.D. 5000 *as performance proceeds.*

Cost estimates are submitted but their function under the CPFF contract is the determination of the fixed fee, based upon a percentage of estimated costs. Article 3(a) of the contracts (R. 77-78) provides for

a fixed fee based upon such a percentage of estimated cost and continues as follows:

> "This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost."

Thus, the contracts expressly recognize the possibility that allowable costs will not be included in the cost estimates, either by reason of error or by reason of conscious omission, and they make provision for the consequences. There is to be no adjustment of fee by reason of such error or omission in the estimates, but the contracts do not provide, and clearly do not contemplate, that costs not included in the estimates shall for that reason cease to be allowable costs under the contracts.

Other provisions of the CPFF contracts not considered by the War Department Board clearly make irrelevant to the contractual obligations the contractor's intention with respect to seeking reimbursement. Each of the CPFF contracts contains a provision that if, prior to final settlement under the contract, T.D. 5000 shall have been amended so as to provide for additional allowable items of cost, "such additional items shall be considered allowable items hereunder." (R. 19)[23] In other words, if respondent in negotiating

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[23] Appendix B, *infra*, pp. 84-85.

the CPFF contracts had not intended to request reimbursement of these items because it had been *correctly* advised that T.D. 5000 did not provide for reimbursement and T.D. 5000 had been subsequently modified to provide reimbursement, then respondent would be entitled to allowance of its claim. Certainly no greater effect should be given to *erroneous* advice concerning T.D. 5000.

Each of the contracts also provides that any cost incurred by the contractor which would constitute an allowable cost under the reimbursement provisions of the contract shall be included in determining the amount payable

> "notwithstanding any provisions contained in the specifications or other documents incorporated in this Contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense or without cost to the Government." (R. 78. See Appendix B pp. 84-85, *infra.*)

In other words, if a written document incorporated in the contract had *expressly* provided that respondent should furnish production tooling or the results of its experimental and development work *without cost to the Government*, the proper charge for these items in accordance with T.D. 5000 *would still be reimbursable.*

The effect of this provision was considered by the War Department Board of Contract Appeals in *Douglas Aircraft Co.*, Nos. 1346 and 1376 (WDBCA 1946). The appellant had contracted with the Corps of Engineers to equip a modification center for the Army Air Forces in the Mojave Desert, California. In seeking a preference rating for materials to build a swimming pool, appellant stated that it pro-

posed to install the pool at its own expense. Later the engineering contract was modified to provide for payment for the pool but the item was disallowed by the Contracting Officer because the modification was subsequent to completion of the pool. Douglas then filed a claim for reimbursement under a CPFF contract which it had entered into with the Army Air Forces for operation of the center. This claim also was denied by the Contracting Officer. The appeal from the first decision was disallowed because not timely, but the cost was allowed under the Air Force operating contract despite the fact that Douglas had not contemplated seeking reimbursement of the cost under this contract and had made no claim for reimbursement until after denial of its claim under the engineering contract. The pertinent part of the opinion is as follows:

> "The first matter for consideration is the statement originally made by appellant's president that the swimming pool would be built at appellant's expense. Such statement was made prior to the execution of the Air Force contract and cannot in any sense be regarded as conclusive against a claim for reimbursement under that contract if the provisions thereto sanction such claim.
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> "Where an expenditure is generally reimbursable under a cost-plus-a-fixed-fee contract it may be excluded from payment only in the event there is a specific contract provision of exclusion. See *Williston on Contracts* (*War Contract Claims*), Vol. 9, Sec. 46, p. 67. Certainly the statement in question had no element of a contract obligation and appellant was not bound to undertake at its expense the construction of a pool, or to complete

one of [sic] begun. Furthermore an integrated contract provision (such as T.D. 5000) would be conclusive against any preliminary understanding of the parties. See *Restatement, Contracts* (1932) Section 230. It is a well settled principle of law that any preliminary negotiations become merged in the written instrument and such instrument is presumed in law to express the final understanding of the parties. See *Simpson* v. *United States*, 172 U.S. 372, 379; Appeal of *McCloskey and Company*, BCA No. 559, 3 CCF 835.

"The most conclusive argument against any contention that the statement of appellant's president expressing willingness to construct the pool at appellant's expense precludes a claim for reimbursement is perhaps to be found in Article 3(b)(16)(d) of Air Force contract recognizing as reimbursable costs the following:

> '(d) Any cost incurred by the Contractor under the terms of this contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this Article shall be included in determining the amount payable under this contract, notwithstanding any provisions contained in the specifications or other documents, incorporated in this contract by reference, designating services to be performed or materials to be furished by the Contractor at its expense or without cost to the Government.'

"Paragraph (b) above referred to, is the provision making T.D. 5000 determinative of allowable costs. If a cost made reimbursable by T.D.

> 5000 is to be paid notwithstanding that some other provision of the contract may have stated it was to be performed or furnished at the contractor's expense then *a fortiori* it should not be held that appellant is precluded from later relying on T.D. 5000 merely because prior to the contract it expressed willingness to bear the cost of constructing the pool. Certainly it would be illogical to give greater effect to a noncontractual expression than is accorded a definite contractual obligation."[24]

The purpose of incorporating a standard such as T.D. 5000 in the CPFF form of contract was to promote uniform cost ascertainment among different contractors.[25] The contracts were written by the petitioner; in fact they were prescribed forms. In treating respondent's intention as a pertinent fact affecting reimbursability of the costs in question, the War Department Board overlooked the underlying purpose and the specific provisions of the CPFF contracts.

It is important to observe that this case is not even one where there was an *understanding* between the parties not expressed in the written contract. Neither the War Department Board nor the lower Court has made a finding that the *petitioner or its agents* intended that the costs would not be claimed or reimbursed.

The most that happened is that at some time some War Department official told someone representing

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[24] This opinion is available at the Army Library.

[25] 1 ASF, PURCHASING POLICIES AND PRACTICES, OFFICIAL HISTORY OF PURCHASES DIVISION 268-71. To further assure uniformity, cost interpretations were issued and the Fiscal Division prepared and distributed a manual of uniform auditing procedures on CPFF contracts. *Id.* at 270-71.

the respondent that such costs "might not be approved for reimbursement under the CPFF contracts." (R. 74) Thus there is not the slightest warrant in the findings or the evidence for the petitioner's statement that "the parties [sic] understood, when the contracts were entered into" that the costs here in question "would not be claimed as reimbursable costs." (Brief, p. 3) The only *intention* found either by Board or Court is the unilateral intention of the respondent. (R. 91, 126)[26]

And, needless to say, the petitioner's statement that this intention existed "when the contracts were entered into" is quite careless—for, as already noted, *supra* pp. 11, 14—two of the CPFF contracts were entered into *after* the first set of vouchers had been submitted, approved by the Contracting Officer, and paid.

Thus the petitioner's case presents in extreme form the proposition that the unilateral intention of one party to a written contract, not reflected in the writing, and never expressed as irrevocable or as a promise either in a technical or in any other sense, shall be seized upon to define contractual obligation.

2. To overrule the lower court would be to disregard basic principles of contract law.

To overrule the lower Court would produce a strange and confusing situation. It is basic to contract law that the clear language of a written agreement is to be

[26] At page 7 of its brief the petitioner states that, "In the course of the negotiations it was understood *by both parties*" that respondent did not intend to charge any of these costs against CPFF production. Three record citations are given, no one of which gives any support for the conclusion that the petitioner knew of the respondent's expectation during the negotiations, much less had an *understanding* that there would be no charge.

interpreted only by reference to the words within the four corners of the contract. This is true even in extreme cases where the actual intent of both parties was entirely different from the meaning of the written words. And this rule has even greater force when the party who drafted the agreement is the party attempting to introduce contrary evidence of subjective intent. *E.g., Calderon* v. *Atlas Steamship Co.*, 170 U.S. 272, 281 (1898); *Moran* v. *Prather*, 23 Wall. 492 (U.S. 1874); *New York Sash & Door Co.* v. *National House & Farms Ass'n, Inc.*, 131 N.J.L. 466, 36 A.2d 891 (1944); 3 WILLISTON, CONTRACTS § 610 (Rev. Ed. 1938). The application of this rule is of vital importance to parties who have taken the pains to reduce their bargain to writing. It is the very purpose of a writing to avoid the misunderstandings so easily born of the vagaries of statements or hints or suggestions made in the course of negotiations, even assuming utmost good faith on both sides.

A keystone principle of contract law will be overthrown, in the law of government contracts, if the lower Court is reversed. For then, under the guise of "all the facts and circumstances"—or, as petitioner puts it, "pertinent facts"—rights will be defined, not by the written memorial, but by statements, actions, and other behavior in the course of negotiation —indeed the mere expectation of a party—even without the slightest evidence of detrimental reliance. No matter how petitioner attempts to argue this issue in its brief, the ultimate fact is that the War Department Board sought to create a new doctrine which would throw an established substantive rule of law out a door labeled "all the facts and circumstances." The lower Court properly refused thus to undermine long established principle.

There remains to say a word about the petitioner's "windfall" argument.

The petitioner states, quite correctly, that the change in amortization for tax purposes resulted in an increase in the respondent's net tax liability for the years 1941 through 1945 of only $32,000. (Brief, p. 9; see also p. 48) What is not quite clear from the petitioner's brief, however, is that this was fortuitous. As of the time the Bureau of Internal Revenue first acted, the respondent had to pay a tax deficiency of $1,337,474.89. (R. 60) Whether taxes for future years would be reduced by an amount largely offsetting this figure depended on whether the entire income earned by the respondent from all sources would suffice to absorb the increased amortization in future years and to reduce normal and excess profits taxes accordingly. A number of contingencies, ranging from a sudden ending of the war to a change in the military's procurement program, might well have left this respondent in a very different condition. It is hardly sound to make rules of law and contract interpretation depend upon "equities" disclosed by long-after-the-event circumstances.

The real "equity" of the case, of course, is that in the absence of countervailing considerations of policy the several branches of the petitioner should deal with a party on a consistent basis. Thus, in renegotiation —where the contracting agency itself takes the action —the government seeks to resolve cost questions in accordance with the determinations of the Bureau of Internal Revenue. 56 STAT. 983 (1942), as amended, 50 U.S.C. App. § 1191(c)(2)(1946). See OFFICE OF THE GENERAL COUNSEL, NAVY CONTRACT LAW 127 (1949). See also H.R. REP. No. 871, 78th Cong., 1st Sess. 36-37 (1943). That happened in this very case

where the Price Adjustment authorities took precisely the same position as did the Bureau with respect to amortization of these costs. (R. 106) There is not the slightest reason for the original contract obligations to be dealt with on a different basis; both law and accounting point to the correctness of the amortization insisted upon by the Bureau. The Price Adjustment Board, in order to give the respondent protection, did finally agree that its recovery of additional amounts in the renegotiation would be contingent upon reimbursement to the respondent of these costs under the CPFF contracts; that action simply underlines the practical necessity that the petitioner's branches act consistently.

If the lower Court is affirmed, respondent and petitioner will be in exactly the position they would have been in had some representative of petitioner not given an erroneous impression to the respondent as to reimbursable costs under T.D. 5000 which led respondent to cut off, on its books, the contracts over which these costs were to be amortized. That matter of bookkeeping did not affect by one cent what the respondent was paid under the fixed price contracts or affect the cost provisions of the CPFF contracts in any way whatever. The lower Court has put the parties exactly where they would stand according to the dictates of T.D. 5000. That is where the petitioner's own form of contract put them, and erroneous bookkeeping, prompted by an early doubt of how T.D. 5000 would be applied, should not be permitted to obscure the obligation framed by the petitioner itself.

To conclude: There is a rather vague suggestion at pp. 30-31 of the petitioner's brief that the CPFF contracts provide that if a cost is *permissible* under T.D. 5000 it *may* be reimbursed but does not *have* to be. We have not been able to follow this argument. Article

3(a) of the contracts provides that, "The Government *will* pay the Contractor . . . the cost . . . ." (R. 77) Article 3(b) provides that, " . . . allowable items of cost *will* be determined by the Contracting Officer in accordance with . . . T.D. 5000 . . . ." (R. 78) And Article 6(a) provides that, "The Government *will* currently reimburse the Contractor for such expenditures made in accordance with Article 3 . . . ." (R. 80) Either T.D. 5000 does or it does not make the costs here reimbursable. If it does not, the lower Court should be reversed. If it does, as we urge, then the respondent has a right to payment; the CPFF contracts certainly do more than merely to confer a privilege on the petitioner to make a payment!

Apparently, in last analysis, the petitioner's argument in this case is that under the contracts a Contracting Officer, in dealing with a T.D. 5000 cost, has discretion to pay or not to pay depending upon "the facts and circumstances." It is hardly to be assumed that any such blank check has been signed by CPFF contractors. The result of the argument to which the petitioner seems to be driven is that T.D. 5000 is no standard at all—save a standard of *exclusion*—and that any *included* cost reflects a *right* only when an unlimited discretion of a Contracting Officer condescends to make it such. Contracting Officers have great power under the contracts prescribed by the Government, as every government contractor knows, but this novel suggestion would create power without any limit whatsoever. Were this Court to adopt the suggestion, it would have translated the Disputes Clauses of government contracts into provisions which, though *professing* to give a contractor access to judicial determination of questions of law, would give complete finality to every decision of the contracting agency.

II

Whether the Experimental and Development Expenses and Production Tooling Costs Were Allowable Under the Provisions of the CPFF Contracts Presented a Question of Interpretation of the Contracts as to Which the Administrative Determination Under the Fact Disputes Clause Was Not Final and Binding.

Each of the CPFF contracts contains a provision that disputes "concerning questions of fact" shall be decided by the Contracting Officer, subject to administrative appeal, and that the decision on appeal shall be "final and conclusive." (R. 80-81) The petitioner agrees that if questions of law are presented the parties are not bound by the decision of the War Department Board. (Petition for Certiorari, pp. 10-11)

A. THIS CASE PRESENTS A STRAIGHTFORWARD QUESTION OF CONTRACT INTERPRETATION.

The petitioner argues that the dispute is "whether the deferred experimental, development and tooling costs were in fact incurred as a necessary incident to the performance of the CPFF contracts" and that, "It is settled that claims involving the ascertainment of cost pose inquiries of fact." (Brief, p. 18) It concludes therefrom that the decision of the War Department Board in this case is final and binding.

In the preceding section of this brief we have discussed the merits of the respondent's claim. Certain matters of fact, of course, are subsidiary to the controverted question involved in that claim—there never was a question of law, including a question of contract interpretation, that could be presented except in the light of some set of facts. Here the facts are: The

experimental work developed the planes produced under the CPFF contracts to exactly the same extent as those produced under the fixed price contracts (R. 95-98); the planes produced throughout were the same (R. 70-71, 77)—the difference between fixed price production and the CPFF production being no more than a difference in the form of contract, not a difference in work done or in the product; the production tools were necessary for and actually devoted to this production (R. 99); the respondent at first did not expect to request reimbursement and kept its books accordingly; then it changed its mind. (R. 82-84)

The only question, then, is whether costs which admittedly are otherwise reimbursable under T.D. 5000 lose that character because the respondent originally did not intend to request reimbursement. The respondent asserts that its intention and related facts are quite irrelevant to the petitioner's contractual obligation to pay set forth in the written agreements; the lower Court agreed with this interpretation of the contracts.

It is submitted that the question, therefore, is not one of a factual inquiry into whether these costs were "incident to the performance of the CPFF contracts" as the petitioner asserts. The War Department Board made no finding that they were not incident to such performance.[27] The question, rather, is a straightfor-

[27] The petitioner appears to intimate that the Board found that there was no "necessary proximate relationship" between the claimed costs and performance of the CPFF contracts. (Brief, p. 29.) Nothing could be more proximate than the actual use of the tools in the production and the actual development from the experimental work of the precise plane produced. In terms of proximation, the relationship to the CPFF P-39 was exactly the same as to the fixed price P-39. The dispute does not concern these matters of physical, technical relationships at all. It is wholly

ward issue of contract interpretation. The lower Court's decision accords with settled legal principles; the Board's view of the matter (and it plainly inferred that a question of law was involved, see *supra* p. 19, n. 18) would import important new principles applicable to the definition of rights and obligations under government contracts.

B. IT IS WELL SETTLED THAT QUESTIONS OF CONTRACT INTERPRETATION ARE NOT DISPUTES CONCERNING QUESTIONS OF FACT WITHIN THE MEANING OF THE FACT DISPUTES CLAUSE.

It need hardly be argued at length that a question of contract interpretation was open to the lower Court. Maddren, *Administrative and Judicial Machinery,* 10 LAW & CONTEMP. PROB. 659, 674 (1944).

That Court early adopted such a view of its powers in determining the finality of decisions made by designated officers under Government contracts. *Lyons* v. *United States,* 30 Ct. Cl. 352, 365 (1895); *Collins and Farwell* v. *United States,* 34 Ct. Cl. 294, 332 (1899). Other Federal courts followed the same rule. *Lewis* v. *Chicago S. F. & C. Ry.,* 49 Fed. 708, 710, 713 (C.C.E.D. Mo. 1891); *King Iron Bridge & Mfg. Co.* v. *St. Louis,* 43 Fed. 768 (C.C.E.D. Mo. 1890), *appeal dismissed,* 149 U.S. 769 (1892).

As a disputes clause covering "disputes concerning questions of fact" came into common use in government contracts, the Court of Claims and other courts interpreting that clause uniformly adhered to the view

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concerned with the consequences of the respondent's bookkeeping from one time to another. Neither the petitioner nor anyone else—least of all the Board—would suggest that there would have been any question here if the amortization in the respondent's bookkeeping at the year end 1941 had embraced the production under the CPFF contracts entered into during that year as it had embraced the fixed price contract entered into in June, 1941.

that departmental decisions on questions of interpretation of the contracts were questions of law for the court rather than questions of fact on which administrative decisions were final and conclusive. *Cramp Shipbuilding Co.* v. *United States,* Ct. Cl. No. 48841, April 8, 1952, Slip Opinion pp. 24-25; *Wunderlich* v. *United States,* 117 Ct. Cl. 92, 212-14 (1951), *rev'd on other grounds,* 342 U.S. 98 (1951); *John McShain, Inc.* v. *United States,* 97 Ct. Cl. 281, 295 (1942); *Rust Engineering Co.* v. *United States,* 86 Ct. Cl. 461, 473-74 (1938); *Davis* v. *United States,* 82 Ct. Cl. 334, 346-47 (1936); *Albina Marine Iron Works, Inc.* v. *United States,* 79 Ct. Cl. 714, 722-23 (1934); *Blair* v. *United States,* 164 F. 2d 115, 116 (5th Cir. 1947), *cert. denied,* 333 U.S. 880 (1948); *United States* v. *Lundstrom,* 139 F. 2d 792, 795 (9th Cir. 1943); *Central Nebraska Public Power & Irrigation District* v. *Tobin Quarries, Inc.,* 157 F. 2d 482, 486 (8th Cir. 1946).

The same view has been entertained by the various contracting agencies which have considered the question. The several Boards of Contract Appeals frequently dismiss appeals involving questions of contract interpretation upon the ground that they are not covered by fact disputes clauses. *Fred A. M. deGroot, Inc.,* 1 CCH CONTRACT CASES FED. 148 (WDBCA 1943); *Central Engineering & Contracting Corp.,* 3 CCH CONTRACT CASES FED. 989 (NDBCA 1945); *Ross Engineering Co.,* 3 CCH CONTRACT CASES FED. 1153 (NDBCA 1945); *St. Louis Shipbuilding & Steel Co.,* 4 CCH CONTRACT CASES FED. ¶ 60,143 (NDBCA 1946); *The Arundel Corp.,* 4 CCH CONTRACT CASES FED. ¶ 60,624 (NDBCA 1948). In other cases, as in this very case, *supra* p. 19, such questions have been considered not upon the ground that they were questions of fact but because by memorandum of the Secretary of War.

10 CODE FED. REGS. § 803.318d(g) (Supp. 1944), the Boards were authorized in their discretion to deal with such questions where the contractor so requested. *Waterman Steamship Corp.*, 5 CCH CONTRACT CASES FED. ¶ 61,222 (ASBCA 1951). The Appeal Board of the Office of Contract Settlement consistently holds that whether a cost is allowable under the terms of a contract is a question of law not covered by the fact disputes clause. *Northwest Airlines, Inc.* v. *Army*, 4 OCSAB 11, 13 (1949); *Northwest Airlines Inc.* v. *Army*, 4 OCSAB 16 (1949); *E. I. du Pont de Nemours & Co.* v. *Army*, 3 OCSAB 201, 204 (1949).

This Court has recognized the Court of Claims's uniform interpretation of fact disputes clauses, and that parties to Government contracts make such contracts in the light of that interpretation. In *United States* v. *Moorman*, 338 U.S. 457 (1950), the contract contained both a standard disputes clause, limited to disputes concerning questions of fact, and an additional disputes clause, not so limited, applicable to specified types of controversies. This Court held that the second clause made decisions thereunder binding as to questions of both law and fact and that it was to be interpreted independently of the fact disputes clause. In this connection Mr. Justice Black stated (338 U.S. at 463):

> "The oft-repeated conclusion of the Court of Claims that questions of 'interpretation' are not questions of fact is ample reason why the parties to the contract should provide for final determination of such disputes by a method wholly separate from the fact-limited provisions of Art. 15."

It is submitted that, in view of the long settled rule that the standard fact disputes clause does not give

finality to decisions on questions of interpretation, use of that clause does not indicate an intention of the parties to submit disputes as to such questions to final determination under that clause. Squarely applicable is the statement in the *Moorman* opinion (338 U.S. at 462) that

> "... the intention of parties to submit their contractual disputes to final determination outside the courts should be made manifest by plain language. *Mercantile Trust Co.* v. *Hensey*, 205 U.S. 298, 309."

But even were this Court inclined to limit that rule, perhaps giving finality to administrative decisions on certain questions such as interpretation of technical specifications, the issue in this case is not of that character. As has already been demonstrated, the error of the War Department Board was its reliance on considerations wholly irrelevant under the written contracts. Even where the broadest finality rule is applicable to an administrative agency, if it employs an improper standard or gives weight to facts excluded from consideration by the terms of the statute under which the agency proceeds, there is presented a question of law fully reviewable by the Courts. *Commissioner* v. *Heininger*, 320 U.S. 467, 475 (1943); *ICC* v. *Railway Labor Executives Ass'n*, 315 U.S. 373, 380 (1942); *Powers* v. *Commissioner*, 312 U.S. 259 (1941); *Southern Pacific Co.* v. *ICC*, 219 U.S. 433, 441, 443, 451-52 (1911); *ICC* v. *Delaware L. & W. R.R.*, 220 U.S. 235, 251 (1911).

Of the cases cited by petitioner on page 28 of its brief, *Trust of Bingham* v. *Commissioner*, 325 U.S. 365 (1945), and *Commissioner* v. *Heininger*, 320 U.S. 467

(1943), strongly support respondent's position. Both held that whether specified facts with respect to expenses otherwise deductible precluded allowance of the deductions under the applicable statutory provisions presented a question of law. Of the remaining cases cited by petitioner on this point,[28] only *Peerless Stages, Inc.* v. *Commissioner,* 125 F. 2d 869 (9th Cir. 1942), deals with a question remotely related to this case. But there the issue was clearly factual—that is whether certain expenses were developmental in nature or were ordinary expenses of current business. In the present case there is no such factual issue.

III

The Respondent's Claim for $1,299,856.02 Is Not Barred for Failure to Exhaust Administrative Remedies

One of petitioner's defenses in the lower Court to the respondent's claim for $1,299,856.02, which had been paid by the petitioner but later recouped, was the respondent's alleged failure to exhaust a remedy provided by the contracts before bringing suit. The petitioner's argument both here and below is that, although the first Contracting Officer had approved the claim, if the second Contracting Officer reconsidered and disapproved it in his decision of March, 1945, then since the respondent's appeal from the latter decision to the WarDepartment Board was allegedly limited to the

[28] Since July 4, 1944, when the Board of Contract Appeals was authorized, in its discretion, to consider questions of law under fact disputes clauses, the fact that the Board considers a case is not indicative that the question involved is one of fact. Of the cases cited on page 29 of petitioner's brief, only the *Chrysler Corporation* case was decided prior to July, 1944. The contract in that case provided that disagreements as to reimbursability should be deemed disputes of fact.

claim based on the vouchers for $986,963.63, the respondent must be taken to have waived its right to sue on the claim for $1,299,856.02.

The lower Court unanimously rejected this technical—not to say unrealistic—defense. The opinion of the majority reasons in two steps: (1) that respondent's claim under the contracts had been determined by the first Contracting Officer and that the petitioner had no right to refuse to honor that determination, absent a showing of "gross mistake, or . . . fraud" (R. 112); and (2) that the decision of the second Contracting Officer actually was not a decision on the claim based on the first set of vouchers, which were not before him, but only on the second set of vouchers which he listed in his decision.

A. THE LOWER COURT PROPERLY HELD THAT THE SECOND CONTRACTING OFFICER NEVER ACTED ON THE FIRST SET OF VOUCHERS COVERING RESPONDENT'S CLAIM FOR $1,299,856.02.

The petitioner's argument is founded upon a misreading of the record. It states that it was "permissible" for the second Contracting Officer to "rectify" the decision of the first Contracting Officer "through recoupment and to disallow the 1¼ million dollar claim." (Brief, p. 34) Then it argues that ". . . approval of vouchers by the second contracting officer providing for recoupment" of the payment of that claim resulted in a dispute under the contracts and that therefore the decision of the second Contracting Officer in March, 1945, was a decision of that dispute, which was not appealed by the respondent. (Brief, p. 42) Again, petitioner asserts that a dispute subject the disputes clause of the contracts arose when "the claim was disapproved and that payment was recouped." (Brief, p. 44)

Thus the whole argument proceeds from an assertion that the second Contracting Officer recouped the original payment; the petitioner's brief goes so far, in the last passage quoted above, as to imply that the second Contracting Officer *first* disapproved the respondent's million and a quarter claim and that *then* the payment was recouped. This version of the facts is based upon footnote 10 at page 34 of the petitioner's brief which mis-states the record and the plain findings of the lower Court.

In that footnote the petitioner states that the second Contracting Officer approved the recoupment, as though he were at that time determining that the previous payment to the respondent had been erroneous. Nothing of the sort happened. We have stated the facts in our Statement of the Case. The second Contracting Officer had pending before him a proposal to recoup by deductions from vouchers otherwise due the respondent. He *eliminated* the deductions for amounts which had *already* been recouped by the Finance Officer pursuant to the Comptroller General's exceptions;[29] and as to $125,000 which had been overlooked in the Comptroller General's formal exceptions, but had been covered in previous informal exceptions, the second Contracting Officer approved a recoupment in that amount "in harmony with the

[29] In support of its statement that the second Contracting Officer took action in September, 1944, to "correct the erroneous" payment to the respondent by approving vouchers for recoupment, the petitioner's brief at p. 34, n. 10, cites Tr. 440. There is an isolated passage in the testimony on this page supporting this statement, but the same witness corrected his own error. (Tr. 446-52) The lower Court's findings follow the corrected testimony. (R. 87)

formal notices of exception and suspension previously received by the Finance Officer" from the Comptroller General. (R. 87) In short, the recoupment was entirely at the direction of the Comptroller General, and the Contracting Officer played no part therein except as to a small amount where his participation was purely formal and a mere reflection of the Comptroller General's action. *Supra* at p. 16. Obviously the second Contracting Officer was not passing any judgment on the question of the propriety of the previous payment to the respondent, for at that time he was still awaiting advice from Wright Field, which did not reach him until November, 1944, and on which he did not act until January, 1945. The recoupment occurred in August and September, 1944. *Supra* at pp. 15-16.

In short, the recoupment in this case represented no action by the second Contracting Officer interpreting or applying the contracts. The recoupment was effected solely at the instance of the Comptroller General whereas the contracts do not contain a single provision conferring any function whatsoever upon the Comptroller General. The representative of the petitioner, and the only person authorized to make determinations under the contracts, was the Contracting Officer.

In January and March, 1945, the second Contracting Officer finally rendered a decision. But the only matter then before him was the second set of vouchers. Under Article 6 of the contracts, he is called upon to approve expenditures for reimbursement only upon verification of certified payrolls, invoices, "or other original papers" presented by the contractor and upon such approval the contractor is to be paid. (R. 80) The second set of vouchers had been presented to him and he rendered his decision thereon; his January decision

specified that his findings were directed to such vouchers, which he listed; and in his re-issued decision of March, he again directed his decision specifically to such vouchers. *Supra* at pp. 17-18. The first set of vouchers was not before him. His opinion, it is true, referred to the entire claim; but that can not alter the fact that the only *action* taken by him was the act of refusing to approve the second set of vouchers pending before him. The lower Court properly so held. (R. 113-14)

B. SINCE RESPONDENT APPEALED THE ONLY DECISION MADE BY THE SECOND CONTRACTING OFFICER, THERE IS NO MERIT TO THE CLAIM THAT IT FAILED TO EXHAUST ITS ADMINISTRATIVE REMEDIES.

The petitioner argues, however, that this decision actually was a redetermination of the respondent's right to reimbursement under its first set of vouchers in view of the fact that the decision does refer to the whole claim. Then, in the next breath, the petitioner argues that the respondent's appeal to the War Department Board did not embrace the claim on the first set of vouchers and that therefore respondent did not exhaust its contractual remedy as to that claim and must be denied judgment therefor solely on that account.

This is, indeed, a highly technical view of the matter. If the claim on the first set of vouchers was covered by the decision of the second Contracting Officer, then it was appealed—for the appeal was from that decision, whatever it was. The parties and the Board construed that decision as involving *action*, as distinguished from the expression of opinion, on the second set of vouchers only and therefore the Board limited its decision to the claim on the second set of vouchers. If this Court now holds that the technicality of the matter was that the decision appealed from was a de-

cision on the whole claim, there is no conceivable basis for holding that the respondent failed to take an appeal—for it *did* appeal from that decision.

Furthermore, the War Department Board dealt with the question before it in terms which were just as applicable to the claim on the first set of vouchers as to the claim on the second set of vouchers. There is not a single fact which has been suggested by the petitioner or relied on by the respondent, with respect to the merits of the issue on the two claims, which is in any way different as between the two. The findings of the Board were just as applicable to the first set of vouchers as to the second set. Consequently the whole question of what the appeal covered is about as academic and hyper-technical as a point urged to this Court could possibly be.[30]

C. ABSENT ANY AUTHORIZATION IN THE CONTRACTS, THE SECOND CONTRACTING OFFICER HAD NO POWER TO REVIEW AND REVERSE THE DETERMINATIONS OF HIS PREDECESSOR.

Finally, we suggest that, in any case, the contracts in question do not contemplate that a second Contracting Officer could recall and redetermine a decision of a previous Contracting Officer (absent fraud or gross mistake) even if it is now to be held that that is what the second Contracting Officer purported to do. Article 6 of the contracts provides that:

> "The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer . . . ." (R. 80)

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[30] Even in applying the doctrine of primary administrative jurisdiction the courts do not require parties to resort to a useless administrative procedure. Montana National Bank v. Yellowstone County, 276 U.S. 499, 505 (1928); Waite v. Macy, 246 U.S. 606, 608-09 (1918).

The contracts may be searched in vain for any suggestion that long after such approval and reimbursement the whole action may be recalled and done over. Cost reimbursement is to be made *currently*. Current cost reimbursement was a matter of basic importance to war contractors faced with the necessity of financing simultaneously enormous current production and expansion of plant facilities.[31] Surely, where the contract provisions in question were written by the petitioner itself, and where the private contractor played no part in their framing, there is no warrant for implying words that are not there—words which would be contradictory to one of the key articles of the CPFF form. For if the petitioner is correct in its argument, every contractor would be placed in the position of being unable to close its books on a single cent of the huge sums involved until years had gone by. And there would be the constant threat of misunderstandings, disputes, and controversy inherent in a situation where Contracting Officers necessarily change, often with frequency, according to the exigencies of military life.

The contracts provide that where the private contractor does not accept a Contracting Officer's determination he *must* appeal within thirty days to the War Department Board. The contracts give the Government no right to appeal for the very good reason that the Contracting Officer is the Government's representative and speaks for the Government. *United States* v. *Mason & Hanger Co.*, 260 U.S. 323, 325

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[31] Hopkins, *Termination Procedure for Army Air Forces*, N.Y.U. Conference on Problems of Termination and Reconversion 55, 58 (1944).

(1922). Just as the Government has no right to appeal, so it has no right to a far more drastic remedy —the remedy of redetermination *at any time* that a new Contracting Officer feels inclined to review his predecessor's decisions. This unlimited right to reopen and revise the past, against the private contractor's very limited right to appeal once and for all within thirty days, not only would read into the contracts provisions which are not there but would accord a degree of liberality to the author of the contracts—the petitioner—which the author does not receive in ordinary private law. *Mutual Life Insurance Co.* v. *Hurni Packing Co.* 263 U.S. 167, 174 (1923). *See Alcoa Steamship Co.* v. *United States,* 338 U.S. 421, 424-25 (1949). There is no reason for the Government to be so favored. Its drafting facilities are quite adequate to write contract forms for its own protection; the courts should not be called upon, long after the event, to read provisions into its contracts.

United States v. *Bentley,* 107 F. 2d 382 (2d Cir. 1939),[32] particularly relied on by the petitioner, is not apposite here, for that case involved an error of fact in the performance of a purely ministerial function. Unquestionably the Contracting Officer is called upon to perform various ministerial functions, such as making mathematical computations, errors in which he or his successor may be competent to correct later. But no such case is presented here. In acting upon the vouchers submitted to him the first Contracting Officer, as the ultimate repository of the government's con-

[32] United States v. Gudewicz, 45 F. Supp. 787 (E.D. N.Y. 1942), simply followed the rule announced in the *Bentley* case.

tracting authority, was required to exercise judgment.[33] Prior to his decision the matter had been debated by the resident auditors; it was obviously a matter of some importance; and the petitioner has not shown that there was any fact overlooked or any relevant consideration ignored. The case is simply one where a successor Contracting Officer arrived at a different conclusion in an area obviously calling for judgment. When Congress confers upon an administrative agency the authority to determine a matter, and the agency acts, it may not thereafter recall its determination and make a new decision simply because it changes its mind. *Cf. Butte, A. & P. Ry.* v. *United States,* 290 U.S. 127, 134-36 (1933); *United States* v. *Seatrain Lines, Inc.,* 329 U.S. 424, 428-29 (1947).[34] Even more clearly, where parties by contract have sought to create machinery for the disposition of commercial relationships between themselves and have provided for their

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[33] Major Richard H. Demuth, *Administration of CPFF Contracts* 1, 4-6 (1944) (lecture presented at AAF Contracting Officers School, Wright Field, Dayton, Ohio, on file at Army Library); Brown, *The Responsibilities, Functions and Duties of a Contracting Officer,* 12 FED. B. J. 236, 237 (1952). Typical sections of respondent's CPFF contracts obviously required the Contracting Officer to exercise his judgment and discretion. See Articles 3(b), 4(b), 5, 6(a), 7(b), 8(b), 16, 27 and 37 of Contract No. W-535 ac 29318, Exhibit K to the Stipulation of Parties, Plaintiff's Exhibit 1 in the certified record.

[34] A similar rule applies in the case of state administrative agencies and officers, which, absent express authorization, have no power to reconsider and overrule previous decisions. Kaliniek v. Collins, 116 Conn. 1, 163 Atl. 460 (1932); Michelson v. Industrial Commission, 375 Ill. 462, 31 N.E.2d 940 (1941); Connors' Case, 121 Me. 37, 115 Atl. 520 (1921); People v. Wemple, 144 N.Y. 478, 39 N.E. 397 (1895); Hylan v. Waldo, 158 App. Div. 654, 143 N.Y. Supp. 901 (1st Dep't 1913).

determination by a specified person at a specified time (in this case reimbursement was intended to be *current*), it hardly comports with their plan to provide that everything determined shall be subject to redetermination at any time. This is doubtless among the considerations which have led the War Department Board in other cases to deny that successor contracting officers may reverse each other from time to time on the same item. *Bell Aircraft Corp.*, 3 CCH CONTRACT CASES FED. 684 (WDBCA 1945); *Dunn Construction Co.*, 4 CCH CONTRACT CASES FED. ¶ 60,478 (WDBCA 1948); *Continental Aviation & Engineering Corp.*, 4 CCH CONTRACT CASES FED. ¶ 60,525 (WDBCA 1948).

Morgan v. *Hines*, 113 F.2d 849 (D.C. Cir. 1940), relied on by the petitioner, presents a quite different problem. There the power of determining issues was given by statute to the head of the agency and he had delegated certain powers to subordinates with authority to make decisions binding upon claimants, subject to a right of appeal to him. The case holds that the claimant in such a situation cannot complain if the head of the agency, without an appeal by the claimant, re-examines the decision of his subordinate and himself makes the determination which is clearly his to make. Under the contracts here involved, the parties have *agreed* that the Contracting Officer shall determine reimbursable costs. Under such a contract provision it is clear that neither that of[illegible]

34a. Compare the long settled view that arbitrators, or persons performing functions in ordinary private contracts similar to those of a government contracting officer, may not redetermine a matter once it has been passed on. Bayne v. Morris, 1 Wall. 97, 99 (U.S. 1863); Mercury Oil Refining Co. v. Oil Workers Int. Union, 187 F.2d 980, 983 (10th Cir. 1951); St. Charles v. Stookey, 154 Fed. 772, 780 (8th Cir. 1907), cert. denied, 208 U.S. 617 (1908); Annotations, 110 A.L.R. [illegible], 142 (1937); 104 A.L.R. 710 (1936); 54 [illegible] 1255, 1266 (1928).

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Ct. Cl. 218, 247-48 (1930); *Burton Coal Co.* v. *United States*, 60 Ct. Cl. 294, 313-14 (1925), *aff'd on another issue*, 273 U.S. 337 (1927). The Comptroller General is not a party to the contracts here in question and his action stands on no different footing from that of any other stranger to the contracts. *Karno-Smith Co.* v. *United States*, 84 Ct. Cl. 110, 124 (1936); *McShain Co.* v. *United States*, 83 Ct. Cl. 405, 409 (1936); *Albina Marine Iron Works, Inc.* v. *United States*, 79 Ct. Cl. 714, 720 (1934); *Penn Bridge Co.* v. *United States*, 59 Ct. Cl. 892, 896 (1924).

Furthermore, it seems to us that the petitioner cannot repudiate the determination of its Contracting Officer in court. This is not a case where there is a showing of negligence or gross mistake by that Officer. *United States* v. *Sutton Chemical Co.*, 11 F.2d 24 (4th Cir. 1926). Rather, it is a case where representatives of the petitioner, other than that Officer, differ with his point of view. But the representative of the petitioner, for the purpose of the contractual dealings, is the Contracting Officer, not the Comptroller General or the Department of Justice. *Supra*, at p. 62. As we have observed, no mistake has been shown, no action based on misinformation. The case is quite similar to that where this Court held that a determination by the Interstate Commerce Commission of the amount to be paid to a railroad during its transition from government to private ownership had to be honored by the Government regardless of differences of view entertained by other representatives of the Government. *United States* v. *Great Northern Ry.*, 287 U.S. 144, 151-53 (1932).

That the contract provision here in question imports finality to the decision of the first Contracting Officer is the holding of *Stewart & Co.* v. *United States*, 71 Ct.

Cl. 126 (1930). The contract there provided that the contractor should be reimbursed "for such of its actual net expenditures in the performance of said work as may be approved or ratified by the contracting officer." The General Accounting Office disallowed certain amounts approved by the Contracting Officer and paid by the disbursing officers and attempted to recover them by counterclaim against a judgment in the contractor's favor. The court held that the determination of the Contracting Officer was binding on the Government, saying (71 Ct. Cl. at 129-30):

> "If the decision of the contracting officer as shown by his approval or ratification was not final, his act in so doing was merely an idle gesture, for the contention of defendant is that notwithstanding such approval it can raise any objection to these items that it sees fit. We do not think the contract can properly be so construed. In fact to so construe it would have the effect to strike from the contract the words 'as may be approved or ratified by the contracting officer,' for they become absolutely useless. . . . The actions of the parties . . . show very plainly that both parties considered that, subject to other provisions in the contract having no bearing on this particular case, the decision made by the contracting officer was final, and such would be the ordinary meaning given to the provision under consideration. It should also be noted in this connection that there is neither allegation nor proof of fraud, bad faith, or palpable disregard of the rights of either party by the contracting officer. So far as it appears from the evidence, he exercised the authority given him with an honest purpose to carry out the

> intention of the parties to the contract and his action was an exercise of the power conferred upon him by that instrument. He discharged that duty by the mutual assent of both parties. The terms by which the power was conferred and the duty imposed are clear and precise and they are susceptible of no other interpretation than that the action of the contracting officer in the matter of expenditures was intended to be conclusive, in the absence of fraud, such gross mistake as would necessarily imply bad faith, or a failure to exercise an honest judgment."

The Court found finality not in any express language to that effect but in the contract provision above quoted. For the reasons already indicated, we believe that the Court's conclusion was correct. It is not the presence in the contract of magic words such as "final and binding", but the intention indicated by a reading of the contract as a whole which is determinative. Where the contract evidences an intention that a specified matter shall be finally decided by a particular officer or agency, this Court holds that the decision of that officer or agency must be recognized as binding, notwithstanding the absence of express language to that effect. *Kihlberg* v. *United States*, 97 U.S. 398 (1878); *United States* v. *Gleason*, 175 U.S. 588 (1900); *Goltra* v. *Weeks*, 271 U.S. 536, 547-48 (1926); *Graham Mfg Co.* v. *United States*, 91 F. Supp. 715 (N.D. Cal. 1950). Furthermore, finality has been given decisions under such contract clauses notwithstanding the presence in the contract of other clauses expressly providing for finality on different matters. *United States* v. *Gleason, supra* at 604. It is submitted that the decisions of the Office of Contract Settlement Appeal Board

cited by the petitioner (Brief, p. 37) are not a correct statement of the law.

The petitioner argues that it would be inequitable for the Government to be bound when the contractor is given the right to appeal under the disputes clause of the contracts on issues of fact and to invoke judicial determination of questions of contract interpretation. But the very fact that the Government is given no right to appeal under the disputes clause demonstrates that it was not intended that the two parties were to be treated in the same way. The interpretation urged by the petitioner would give the Government an unlimited right to repudiate its Contracting Officers' determinations, while the private contractor is held to a precise procedure which must be pursued within a brief period of time or be lost forever. *Barnes Construction Co.*, 3 CCH CONTRACT CASES FED. 553 (WDBCA 1945); *Goldschmidt & Bethune Co.*, 3 CCH CONTRACT CASES FED. 381 (WDBCA 1945); *N. P. Severin Co.*, 2 CCH CONTRACT CASES FED. 771 (WDBCA 1944); *A. C. Campbell Co.*, 1 CCH CONTRACT CASES FED. 776 (WDBCA 1943); *John T. Brady & Co.*, 1 CCH CONTRACT CASES FED. 772 (WDBCA 1943). The more reasonable interpretation is that the difference in treatment means that the Government is to be bound by the determinations of its own Contracting Officer, appointed, advised, and disciplined by it.

An alternative view is that the determinations of its Contracting Officer will bind the Government on issues of fact, with both parties free to invoke judicial determination of issues of contract interpretation. The contractor may invoke the courts on disputes of law because the contracts do not foreclose that avenue; it is only on fact disputes that the War Department process is conclusive. It might be argued that the

Government is similarly free to seek the courts' decisions of questions of contract interpretation, and that the failure to provide the Government with the remedy on issues of fact which is extended to the contractor under the fact disputes clause implies that on such issues—but only on such issues—the Contracting Officer's determinations settle the question as to the Government. This suggestion is not as consistent with the contractual pattern as is the view that the Government is bound both on fact and law—but it at least has the merit of preserving a contractual relationship which does not weigh the scales wholly against the contractor and in favor of the Government. If this latter view is adopted, and if the petitioner is correct in its argument that the question in this case is one of fact, it follows that the petitioner is bound by the first Contracting Officer's decision on the first set of vouchers.

Of course, if we are correct in our argument that the dispute here is one of law, the petitioner's plea that the contractual remedy for fact disputes has not been exhausted can have no application.[35] In no event, however, can there be any merit in the claim that the respondent has tripped over a technicality; the essence of the matter is that the respondent appealed from the decision of the second Contracting Officer—whatever it was—and that is all that it could have done.

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[35] United States v. Lundstrom, 139 F. 2d 792 (9th Cir. 1943); Cramp Shipbuilding Co. v. United States, Ct. Cl. No. 48841, April 8, 1952, Slip Opinion p. 25; Pottsville Casting & Machine Shops, Inc. v. United States, Ct. Cl. No. 49092, December 4, 1951, Slip Opinion pp. 26-27; Paretta Contracting Co. v. United States, 109 Ct. Cl. 324, 351-52 (1947), *cert. denied*, 333 U.S. 832 (1948).

CONCLUSION

Wherefore, it is respectfully submitted that the judgment of the Court below should be affirmed.

Respectfully submitted,

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APPENDIX A

PERTINENT PROVISIONS OF T. D. 5000, 1940-2 CUM. BULL. 397, 404-409:

SEC. 26.9. *Cost of performing a contract or subcontract.*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract; and (2) the proper proportion of any indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.

(b) *Elements of cost.*—No definitions of the elements of cost may be stated which are of invariable application to all contractors and subcontractors. In general, the elements of cost may be defined for purposes of the Act as follows:

(1) Manufacturing cost, which is the sum of factory cost (see paragraph (c) of this section) and other manufacturing cost (see paragraph (d) of this section);

(2) Miscellaneous direct expenses (see paragraph (e) of this section);

(3) General expenses, which are the sum of indirect engineering expenses, usually termed "engineering overhead" (see paragraph (f) of this section) and expenses of distribution, servicing and administration (see paragraph (g) of this section); and

(4) Guarantee expenses (see paragraph (h) of this section).

(c) *Factory cost.*—Factory cost is the sum of the following:

(1) *Direct materials.*—Materials, such as those purchased for stock and subsequently issued for contract operations and those acquired under subcontracts, which become a component part of the finished product or which are used directly in fabricating, converting or processing such materials or parts.

(2) *Direct productive labor.*—Productive labor, usually termed "shop labor," which is performed on and is properly chargeable directly to the article manufactured or constructed pursuant to the contract or subcontract, but which ordinarily does not include direct engineering labor (see subparagraph (3) of this paragraph).

(3) *Direct engineering labor.*—The compensation of professional engineers and other technicists (including reasonable advisory fees), and of draftsmen, properly chargeable directly to the cost of the contract or subcontract.

(4) *Miscellaneous direct factory charges.*—Items which are properly chargeable directly to the factory cost of performing the contract or subcontract but which do not come within the classifications in subparagraphs (1), (2), and (3) of this paragraph, as for example, royalties which the contracting party pays to another party and which are properly chargeable to the cost of performing the contract or subcontract (but see paragraph (d) of this section).

(5) *Indirect factory expenses.*—Items, usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

(A) *Labor.*—Amounts expended for factory labor, such as supervision and inspection, clerical labor, timekeeping, packing and shipping, stores supplies, services of tool crib attendants, and services in the factory employment bureau, which are not chargeable directly to productive labor of the contract or subcontract.

(B) *Materials and supplies.*—The cost of materials and supplies for general use in the factory in current operations, such as shop fuel, lubricants, heat-treating, plating, cleaning and anodizing supplies, nondurable tools and gauges, stationery (such as time tickets and other forms), and boxing and wrapping materials.

(C) *Service expenses.*—Factory expenses of a general nature, such as those for power, heat and light (whether purchased or produced), ventilation and air-conditioning and operation and maintenance of general plant assets and facilities.

(D) *Fixed charges and obsolescence.*—Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable stand-by equipment; and depreciation and obsolescence of special equipment facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the department concerned has made a certification binding upon the Commissioner of Internal Revenue, pursuant to section 4 of the Act, in the case of such contract or subcontract. See Executive Order No. 8465 and Joint Rules issued under such Order (page 385, this Bulletin). In making allowances for depreciation, consideration shall be given to the number and length of shifts.

(E) *Miscellaneous indirect factory expenses.*—Miscellaneous factory expenses not directly chargeable to the factory cost of performing the contract or subcontract, such as purchasing expenses; ordinary and necessary expenses of rearranging facilities within a department or plant; employees' welfare expenses; premiums or dues on compensation insurance; employers' payments to unemployment, old age and social security Federal and State funds not including payments deducted from or chargeable to employees or officers; pensions and retirement payments to factory employees; factory accident compensation (as to self-insurance, see paragraph (g) of this section); but not including any amounts which are not incident to services, operations, plant, equipment or facilities involved in the performance of the contract or subcontract.

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and de-

velopment charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

(e) *Miscellaneous direct expenses.*—Miscellaneous direct expenses as used in paragraph (b) of this section include—

(1) *Cost of installation and construction.*—Cost of installation and construction includes the cost of materials, labor, and expenses necessary for the erection and installation prior to the completion of the contract and after the delivery of the product or material manufactured or constructed pursuant to the contract or subcontract.

(2) *Sundry direct expenses.*—Items of expense which are properly chargeable directly to the cost of performing a contract or subcontract and which do not constitute guarantee expenses (see paragraph (h) of this section) or direct costs classified as factory cost or other manufacturing cost (see paragraphs (c) and (d) of this section), such as premiums on performance or other bonds required under the contract or subcontract; State sales taxes imposed on the contracting party; freight on outgoing shipments; fees paid for wind tunnel and model basin tests; demonstration and test expenses; crash insurance premiums; traveling expenses. In order for any such item to be allowed as a charge directly to the cost of performing a contract or sub-

contract, (1) a detailed record shall be kept by the contracting party of all items of a similar character, and (2) no item of a similar character which is properly a direct charge to other work shall be allowed as a part of any indirect expenses in determining the proper proportion thereof chargeable to the cost of performing the contract or subcontract. As to allowable indirect expenses, see paragraphs (e) (5), (f), (g), and (j) of this section.

(f) *Indirect engineering expenses.*—Indirect engineering expenses, usually termed "engineering overhead," which are treated in this section as a part of general expenses in determining the cost of performing a contract or subcontract (see paragraph (b) of this section), comprise the general engineering expenses which are incident to and necessary for the performance of the contract or subcontract, such as the following:

(1) *Labor.*—Reasonable fees of engineers employed in a general consulting capacity, and compensation of employees for personal services to the engineering department, such as supervision, which is properly chargeable to the contract or subcontract, but which is not chargeable as direct engineering labor (see paragraph (e) (3) of this section).

(2) *Material.*—Supplies for the engineering department, such as paper and ink for drafting and similar supplies.

(3) *Miscellaneous expenses.*—Expenses of the engineering department, such as (A) maintenance and repair of engineering equipment, and (B) services purchased outside of the engineering department for blue printing, drawing, computing, and like purposes.

(g) *Expenses of distribution, servicing, and administration.*—Expenses of distribution, servicing, and administration, which are treated in this section as a part of general expenses in determining the cost of performing a contract or subcontract (see paragraph (b) of this section), comprehend the expenses incident to and necessary for the performance of the contract or subcontract, which are incurred in connection with the distribution and general servicing of the contracting party's products and the general administration of the business, such as—

(1) *Compensation for personal services of employees.*—The salaries of the corporate and general executive officers

and the salaries and wages of administrative clerical employees and of the office services employees such as telephone operators, janitors, cleaners, watchmen, and office equipment repairmen.

(2) *Bidding and general selling expenses.*—Bidding and general selling expenses which by reference to all the pertinent facts and circumstances reasonably constitute a part of the cost of performing a contract or subcontract. The treatment of bidding and general selling expenses as a part of general expenses in accordance with this paragraph is in lieu of any direct charges which otherwise might be made for such expenses. The term "bidding expenses" as used in this section includes all expenses in connection with preparing and submitting bids.

(3) *General servicing expenses.*—Expenses which by reference to all the pertinent facts and circumstances reasonably constitute a part of the cost of performing a contract or subcontract and which are incident to delivered or installed articles and are due to ordinary adjustments or minor defects; but including no items which are treated as a part of guarantee expenses (see paragraph (h) of this section) or as a part of direct costs, such as direct materials, direct labor, and other direct expense.

(4) *Other expenses.*—Miscellaneous office and administrative expenses, such as stationery and office supplies; postage; repair and depreciation of office equipment; contributions to local charitable or community organizations to the extent constituting ordinary and necessary business expenses; employees' welfare expenses; premiums and dues on compensation insurance; employers' payments to unemployment, old age, and social security Federal and State funds, not including payments deducted from or chargeable to employees or officers; pensions and retirement payments to administrative office employees and accident compensation to office employees (as to self-insurance, see the following subparagraph).

Subject to the exception stated in this subparagraph, in cases where a contracting party assumes its own insurable risks (usually termed "self-insurance"), losses and payments will be allowed in the cost of performing a contract or subcontract only to the extent of the actual losses suffered or payments incurred during, and in the course

of, the performance of the contract or subcontract and properly chargeable to such contract or subcontract. If, however, a contracting party assumes its own insurable risks (a) for compensation paid to employees for injuries received in the performance of their duties, or (b) for unemployment risks in States where insurance is required, there may be allowed as a part of the cost of performing a contract or subcontract a reasonable portion of the charges set up for purposes of self-insurance under a system of accounting regularly employed by the contracting party, as determined by the Commissioner of Internal Revenue, at rates not exceeding the lawful or approved rates of insurance companies for such insurance, reduced by amounts representing the acquisition cost in such companies, provided the contracting party adopts and consistently follows this method with respect to self-insurance in connection with all contracts and subcontracts subsequently performed by him.

Allowances for interest on invested capital are not allowable as costs of performing a contract or subcontract.

Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such cost, are the following: Entertainment expenses; dues and memberships other than of regular trade associations; donations except as otherwise provided above; losses on other contracts; profits or losses from sales or exchanges of capital assets; extraordinary expenses due to strikes, or lockouts; fines and penalties; amortization of unrealized appreciation of values of assets; expenses, maintenance and depreciation of excess facilities (including idle land and building, idle parts of a building, and excess machinery and equipment) vacated or abandoned, or not adaptable for future use in performing contracts or subcontracts; increases in reserve accounts for contingencies, repairs, compensation insurance (except as above provided with respect to self-insurance) and guarantee work; Federal and State income and excess-profits taxes and surtaxes; cash discount earned up to 1 per cent of the amount of the purchase, except that all discounts on subcontracts subject to the Act will be considered; interest incurred or earned; bond discount or finance charges; premiums for life insurance on the lives of officers; legal and accounting fees in connection with reorganizations, security issues, capital stock issues, and the prosecution

of claims against the United States (including income tax matters); taxes and expenses on issues and transfers of capital stock; losses on investments; bad debts; and expenses of collection and exchange.

In order that the cost of performing a contract or subcontract may be accounted for clearly, the amount of any excess profits repayable to the United States pursuant to the Act should not be charged to or included in such cost.

(h) *Guarantee expenses.*—Guarantee expenses include the various items of factory cost, other manufacturing cost, cost of installation and construction, indirect engineering expenses, and other general expenses (see paragraphs (e) to (g), inclusive, of this section) which are incurred after delivery or installation of the article manufactured or constructed pursuant to the particular contract or subcontract and which are incident to the correction of defects or deficiencies which the contracting party is required to make under the guarantee provisions of the particular contract or subcontract. If the total amount of such guarantee expenses is not ascertainable at the time of filing the report required to be filed with the collector of internal revenue (see section 26.16 of these regulations) and the contracting party includes any estimated amount of such expenses as part of the claimed total cost of performing the contract or subcontract, such estimated amount shall be separately shown on the report and the reasons for claiming such estimated amount shall accompany the report; but only the amount of guarantee expenses actually incurred will be allowed. If the amount of guarantee expenses actually incurred is greater than the amount (if any) claimed on the report and the contracting party has made an overpayment of excess profit, a refund of the overpayment shall be made in accordance with the provisions of section 26.19 of these regulations. If the amount of guarantee expenses actually incurred is less than the amount claimed on the report and an additional amount of excess profit is determined to be due, the additional amount of excess profit shall be assessed and paid in accordance with the provisions of section 26.19 of these regulations.

(i) *Unreasonable compensation.*—The salaries and compensation for services which are treated as a part of the cost of performing a contract or subcontract include rea-

sonable payments for salaries, bonuses, or other compensation for services. As a general rule, bonuses paid to employees (and not to officers) in pursuance of a regularly established incentive bonus system may be allowed as a part of the cost of performing a contract or subcontract. The test of allowability is whether the aggregate compensation paid to each individual is for services actually rendered incident to, and necessary for, the performance of the contract or subcontract, and is reasonable. Excessive or unreasonable payments whether in cash, stock, or other property ostensibly as compensation for services shall not be included in the cost of performing a contract or subcontract.

(j) *Allocation of indirect costs.*—No general rule applicable to all cases may be stated for ascertaining the proper proportion of the indirect costs to be allocated to the cost of performing a particular contract or subcontract. Such proper proportion depends upon all the facts and circumstances relating to the performance of the particular contract or subcontract. Subject to a requirement that all items which have no relation to the performance of the contract or subcontract shall be eliminated from the amount to be allocated, the following methods of allocation are outlined as acceptable in a majority of cases:

(1) *Factory indirect expenses.*—The allowable indirect factory expenses (see paragraph (c) (5) of this section) shall ordinarily be allocated or "distributed" to the cost of the contract or subcontract on the basis of the proportion which the direct productive labor (see paragraph (c) (2) of this section) attributable to the contract or subcontract bears to the total direct productive labor of the production department or particular section thereof during the period within which the contract or subcontract is performed, except that if the indirect factory expenses are incurred in different amounts and in different proportions by the various producing departments consideration shall be given to such circumstances to the extent necessary to make a fair and reasonable determination of the true profit and excess profit.

(2) *Engineering indirect expenses.*—The allowable indirect engineering expenses (see paragraph (f) of this section) shall ordinarily be allocated on "distributed" to the cost of the contract or subcontract on the basis of the

proportion which the direct engineering labor attributable to the contract or subcontract (see paragraph (c) (3) of this section) bears to the total direct engineering labor of the engineering department or particular section thereof during the period within which the contract or subcontract is performed. If the expenses of the engineering department are not sufficient in amount to require the maintenance of separate accounts, the engineering indirect costs may be included in the indirect factory expenses (see paragraph (c) (5) of this section) and allocated or distributed to the cost of performing the contract or subcontract as a part of such expenses, provided the proportion so allocated or distributed is proper under the facts and circumstances relating to the performance of the particular contract or subcontract.

(3) *Administrative expenses (or "overhead").*—The allowable expenses of administration (see paragraph (g) of this section) or other general expenses except indirect engineering expenses, bidding and general selling expenses, and general servicing expenses shall ordinarily be allocated or distributed to the cost of performing a contract or subcontract on the basis of the proportion which the sum of the manufacturing cost (see paragraph (b) of this Section) and the cost of installation and construction (see paragraph (e) of this section) attributable to the particular contract or subcontract bears to the sum of the total manufacturing cost and the total cost of installation and construction during the period within which the contract or subcontract is performed.

(4) *Bidding, general selling, and general servicing expenses.*—The allowable bidding and general selling expenses and general servicing expenses (see paragraph (g) (2) and (3) of this section) shall ordinarily be allocated or distributed to the cost of performing a contract or subcontract on the basis of—

(i) The proportion which the contract price of the particular contract or subcontract bears to the total sales made (including contracts or subcontracts completed) during the period within which the particular contract or subcontract is performed, or

(ii) The proportion which the sum of the manufacturing cost (see paragraph (b) of this section) and the cost of installation and construction (see paragraph

(e) of this section) attributable to the particular contract or subcontract bears to the sum of the total manufacturing cost and the total cost of installation and construction during the period within which the contract or subcontract is performed.

except that special consideration shall be given to the relation which certain classes of such expenses bear to the various classes of articles produced by the contracting party in each case in which such consideration is necessary in order to make a fair and reasonable determination of the true profit and excess profit. See section 26.14 of these regulations.

APPENDIX B

Pertinent Provisions of the CPFF Countries

With minor variations in phrasing each of the CPFF contracts contain provisions substantively identical to those in Contract No. W 535 ac-20910 as follows:

"Article 3—Consideration

"(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the contract, subject to reimbursement for cost as outlined in Article 6 hereof, the cost, plus a fixed fee of . . . being . . . percent of the total estimated cost . . . . This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

"(b) For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

"(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract, would have been considered as allowable items of cost within the meaning of said regulations, shall be considered as allowable items of cost incurred hereunder.

"(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this contract, notwithstanding any provisions contained in the specifications or other documents incorporated

in this contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense or without cost to the Government.

"In the event that prior to final settlement under this contract such regulations [T. D. 5000] be amended so as to provide for additional allowable items of cost such additional items shall be considered allowable items hereunder.*

"(c) The Contractor shall, to the extent of his ability, procure materials and services at the most advantageous prices available with due regard to securing prompt delivery of satisfactory materials, take all cash and trade discounts, rebates, allowances, credits, salvage, commissions and bonifications, and when unable to take advantage of such benefits he shall promptly notify the Contracting Officer to that effect and the reason therefor. In determining the actual net cost of articles and materials of every kind required for the purpose of this contract, there shall be deducted from the gross cost thereof all cash and trade discounts, rebates, allowances, credits, salvage, commissions and bonifications which have accrued to the benefit of the Contractor or would have so accrued except for the fault or neglect of the Contractor. Such benefits lost through no fault or neglect on the part of the Contractor, or lost through fault of the Government, shall not be deducted from gross costs."

* * *

"ARTICLE 6—PAYMENTS

"(a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 as may be approved or ratified and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers. Provided, however, that subject to the requirement of paragraph (c) of Article 7 hereof, in respect of

* In the case of Contracts Nos. W 535 ac-29318 and W 535 ac-40071 the provision specifically covers amendments of T. D. 5000 "before or after" the effective date of the contract. The provision in Contract No. DA-W 535 ac-156 refers to changes "on or before" the effective date. It is apparent that this is a typographical error, since such language deprives the provision of any real effect.

the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this article. Generally, reimbursement will be made weekly but may be made at more frequent intervals if the conditions so warrant.

"(b) *Payment of the Fixed Fee.* Ninety per cent (90%) of the fixed fee of Six per cent (6%) set forth in paragraph (a) of Article 3 hereof, shall be paid as it accrues, in monthly installments based upon the percentage of the completion of the work as determined from estimates made and approved by the Contracting Officer. Upon completion of the work and its final acceptance, any unpaid balance of the fee, including the additions thereto, if any, to which the Contractor may be entitled, as provided in said paragraph (a) of Article 3, shall be paid to the Contractor."

Contracts No. W 535 ac-20910, DA-W 535 ac-156 and W 535 ac-29318 contain this additional section in Article 6:

"(c) *Advances*—Advance payments may be made from time to time for the supplies called for, when the Secretary of War deems such action necessary in the interest of national defense: *Provided, However,* That the total amount of money so advanced shall not exceed thirty per centum (30%) of the contract price of the articles called for that such advances, as made, shall be upon such terms and conditions and with such adequate security as the Secretary of War shall prescribe."

Contract No. W 535 ac-40071 contains these additional sections in Article 6:

"(c) As of the date of the execution of this contract there has been allotted for it the total sum of .... This sum may be increased from time to time by the Government solely in its discretion. Upon the making of any such increase the Contracting Officer shall notify the Contractor in writing of the amount of such increase.

"(d) Notwithstanding any other provisions of this contract the Contractor shall not be bound to take any action in connection with the performance of this contract that would

cause the amount for which the Government will be obligated hereunder to exceed the sum allotted for this contract, and the obligation of the Contractor to proceed with the performance of this contract shall be limited accordingly. If at any time the Contractor has reason to believe that the amount to be expended by it in the next succeeding 30 days, when added to all previous expenditures and to the total amount of the Contractor's fixed-fee, will exceed the sum allotted for this contract, it shall notify the Contracting Officer to that effect, giving a new estimate of its total expenditures under this contract, so that an appropriate increase may be made in the sum allotted for this contract. Anything in this contract to the contrary notwithstanding, the Government shall not be obligated to pay to the Contractor either for reimbursement of expenditures or fixed fee or otherwise any amount in excess of the sum allotted for this contract; provided, however, that if the Contractor makes any expenditures for which funds are not allotted, the Contracting Officer may ratify such expenditures when funds are allotted."

Contract No. DA-W 535 ac-156 contains the following disputes clause:

"ARTICLE 16—DISPUTES

"Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance."

Contracts Nos. W 535 ac-20910 and W 535 ac-29318 originally contained the same short form clause, but apparently supplemental agreements omitted from the certified record substituted the following clause, also contained in Contract No. W 535 ac-40071 (see R. 28):

"ARTICLE 16—DISPUTES

"Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail

a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or the president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract."

APPENDIX C

PERTINENT EXHIBITS

Plaintiff's Exhibit 25

COPY

WAR DEPARTMENT
ARMY AIR FORCES

Material Center
Eastern Procurement Division
Office of the Army Air Forces Representative
Bell Aircraft Corporation, Niagara Frontier Division

Capt. H. B. Davies
bmd: Contracting Officer
10 January 1945

SUBJECT: Amortization Costs Incurred
on Experimental Contracts

To: Bell Aircraft Corporation
2050 Elmwood Avenue
Buffalo 7, New York

1. Forwarded herewith is a copy of a decision made by the Chief of the Procurement Division of the Air Technical Service Command on the reimbursement of amortization of development and experimental expense over CPFF contracts.

2. This office incorporates the decision of the Chief of the Procurement Division as a finding of facts in denying reimbursement to the contractor for this expenditure, as requested on Audit Bureau Vouchers, as follows:

Voucher No.	Contract No.	Amount
8449	W535 ac 40071	$ 29,102.96
8450	"	67,973.28
8445	"	11,774.48
8446	"	27,500.64
8447	"	29,880.52
8448	"	69,789.36
8439	W535 ac 20910	20,495.76
8440	"	8,775.32
8441	"	1,037.76
8442	"	444.32

Voucher No.	Contract No.	Amount
8443	W535 ac 29318	499.86
8444	"	722.02
*70-131	W535 ac 20910	22,874.70
*70-130	"	35,582.98
*70-72	W535 ac 40071	39,395.44
*70-128	W535 ac 20910	72,676.10
*70-129	"	113,052.07
*70-71	W535 ac 40071	125,164.76
10619	DA W535 ac 156	4,371.50
10620	W535 ac 29318	55,916.00
10621	W535 ac 40041	13,979.04
10606	DA W535 ac 156	13,888.85
10607	W535 ac 29318	177,652.86
10608	W535 ac 40041	44,413.35

NOTE: * Terminated Contracts.

/s/ H. B. DAVIES
H. B. DAVIES
Captain, Air Corps
Contracting Officer

cc: Resident Auditor
Incl. (1)
1. WF ltr. 11.13.44

COPY

ARMY AIR FORCES
HEADQUARTERS

AIR TECHNICAL SERVISCE COMMAND

TSBCO3/JGH/aed
Wright Field, Dayton, Ohio
13 November 1944

SUBJECT: Amortization Costs Incurred on Experimental Contracts

TO: District Supervisor
Eastern Procurement District
Air Technical Service Command
67 Broad Street
New York 4, New York
Attention: Chief, Contract Section

1. Reference is made to letter dated 10 December 1943 from the Bell Aircraft Corporation Resident Auditor to the District Auditor, Eastern Procurement District, sub-

ject "Amortization of Losses on Fixed Price Contracts" and to an audit report attached thereto prepared by the Resident Auditor concerning the manner in which Bell Aircraft Corporation has amortized over certain fixed price contracts with the United States Government and with the British Government the sum of $3,422,870.23. The said letter of 10 December 1943, the report attached thereto, and the opinion of the District Auditor to the Resident Auditor on the matter dated 30 September 1943 together with a statement by Bell Aircraft Corporation dated 5 January 1944 concerning the same matter were forwarded by your office to this Headquarters by 1st Indorsement dated 20 January 1944, subject as above, for the views of this office as to the right of Bell to be reimbursed under its CPFF contracts for any portion of the said amount.

2. It appears from such information forwarded to this Headquarters that during the years 1938, 1939, and 1940, Bell Aircraft Corporation expended a sum of $3,422,870.23 in connection with the development of experimental airplanes XP-39, XFM-1 and XFL-2, and that the prices of fixed price experimental contracts held by Bell with the Government were insufficient to cover any portion of such expenditures. It further appears that the said sum of $3,422,870.23 was fully amortized by Bell Aircraft Corporation over certain fixed price production contracts between it and the United States Government and between it and the British Government during the years 1940, 1941, and 1942. It also appears from 5th Indorsement from the Resident Auditor, Bell Aircraft Corporation, to the Contracting Officer, Bell Aircraft Corporation dated 27 July 1944, concurred in by the Contracting Officer at Bell by 6th Indorsement dated 28 July 1944, that Bell Aircraft Corporation earned total aggregate net profits applicable to the said fixed price production contracts of $17,590,201.57. The profits earned on the said fixed price production contracts, therefore, are more than enough to recover for Bell Aircraft Corporation the total amount of the expenditures of $3,422,870.23 referred to above, and were so treated on the books of Bell Aircraft Corporation.

3. It appears that in 1943 as a result of conferences with the Internal Revenue Department, Bell Aircraft Corporation revised its formal method of amortizing the said costs of $3,422,870.23 against fixed price production contracts only and spread the amounts of such costs over all of its fixed

price and CPFF contracts for airplanes which Bell claims benefitted from the development work which it did. As a result, the amount of $3,422,870.23, adjusted to $3,374,465.00 by the elimination of certain overhead items was charged by Bell in 1943 against fixed price contracts and cost-plus-a-fixed-fee contracts as follows:

a. Against fixed price contracts.....	$1,087,645.05
b. Against CPFF contracts	2,286,819.95
Total	3,374,465.00

4. It also appears from letter to the District Supervisor, Eastern Procurement District, from the Contracting Officer at Bell Aircraft Corporation dated 5 June 1944, subject as above, that Bell Aircraft Corporation has already been reimbursed by the Government under its CPFF contracts for $1,299,855.92 of the amount of $2,286,819.95 noted above and that the General Accounting Office, by informal exceptions No. 777, 778, and 779, has raised the question of whether such amounts were properly reimbursed to Bell. It also appears from the letter of Bell Aircraft Corporation dated 5 January 1944 and referred to in paragraph 1 that Bell Aircraft Corporation has submitted, or is proposing to submit, claims for reimbursement under its CPFF contracts for the balance of the sum of $2,286,819.95.

5. By letter dated 30 October 1944, subject "Amortization of Development Expenses on CPFF Contracts" directed to the Bell Aircraft Corporation Contracting Officer, Bell states that it did not include in its quotations on fixed price production contracts referred to in paragraph 2 over which it originally amortized the development costs of $3,422,-870.23, the entire amount of such expenditures, but Bell does not indicate how much of such expenditures were, in fact, included in its fixed price quotations, and has failed to furnish any information which indicates that, notwithstanding the views of the Resident Auditor and the Contracting Officer stated in paragraph 2, it did not, in fact, recover through the fixed price production contracts referred to in paragraph 2 of the entire amount of such development expenses.

6. It appears that the said sum of $2,286,819.95 which Bell has charged on its books against CPFF contracts does not, in fact, represent costs of performing such CPFF contracts and that reimbursement for such costs under the said CPFF contracts would result in Bell's receiving double

payment from the Government therefor. It is therefore the opinion of this Headquarters that Bell is not entitled to reimbursement under its CPFF contracts for P-39 and P-63 airplanes for any portion of the said sum of $2,286,-819.95.

By Command of Lieutenant General KNUDSEN:

ORVAL R. COOK
Brig. General, U. S. A.
Chief, Procurement Division.

copy

Plaintiff's Exhibit 26

Capt. H. B. Davies
bmd; Contracting Officer

WAR DEPARTMENT
ARMY AIR FORCES
AIR TECHNICAL SERVICE COMMAND
EASTERN DISTRICT
OFFICE OF THE ARMY AIR FORCES REPRESENTATIVE

1 March 1945

Bell Aircraft Corporation, Niagara Frontier Division

SUBJECT: Findings of Fact and Decision of Contracting Officer

To: Bell Aircraft Corporation
2050 Elmwood Avenue
Buffalo 7, N. Y.

The finding of fact and decision of the Contracting Officer regarding amortization costs incurred on Experimental contracts as cited in letter from this office dated 10 January 1945 has been rescinded, and a new findings of fact and decision of the Contracting Officer is forwarded herewith.

/s/ H. B. DAVIES
H. B. DAVIES
Captain, Air Corps
Contracting Officer

Incl. (1)
Contracting Officer's ltr. dated 1 March 1945 cc: Resident Auditor

Capt. H. B. Davies
bmd; Contracting Officer

WAR DEPARTMENT
ARMY AIR FORCES
AIR TERMINAL SERVICE COMMAND
EASTERN DISTRICT
OFFICE OF THE ARMY AIR FORCES REPRESENTATIVE

1 March 1945

Bell Aircraft Corporation, Niagara Frontier Division

SUBJECT: Finding of Fact and Decision of Contracting Officer

To: Bell Aircraft Corporation
2050 Elmwood Avenue
Buffalo 7, N. Y.

1. As Contracting Officer of AAF under your Contract numbers W535 ac 40071, 20910, 29318, 40041, and DA W535 ac 156, Audit Voucher numbers as listed below, I find as fact:

Voucher No.	Contract No.	Amount
8449	W535 ac 40071	$ 29,102.96
8450	"	67,973.28
8445	"	11,774.48
8446	"	27,500.64
8447	"	29,880.52
8448	"	69,789.36
8439	W535 ac 20910	20,495.76
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8442	"	444.32
8443	W535 ac 29318	499.86
8444	"	722.02
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70-72*	W535 ac 40071	39,395.44
70-128*	W535 ac 20910	72,676.10
70-129*	"	113,052.07
70-71*	W535 ac 40071	125,164.76
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10606	DAW535 ac 156	13,888.85
10607	W535 ac 29318	177,652.86
10608	W535 ac 40041	44,413.35

* Terminated Contracts.

a. That during the years 1938, 1939, and 1940, Bell Aircraft Corporation expended a sum of $3,422,870.23 in connection with the development of experimental airplanes XP-39, XFM-1 and XFL-2, and that the prices of fixed price experimental contracts held by Bell with the Government were insufficient to cover any portion of such expenditures. It further appears that the said sum of $3,422,870.23 was full amortized by Bell Aircraft Corporation over certain fixed price production contracts between it and the United States Government and between it and the British Government during the years 1940, 1941, and 1942. It also appears that Bell Aircraft Corporation earned total aggregate net profits applicable to the paid fixed price production contracts of $17,590,201.57. The profits earned on the said fixed price production contracts, therefore, are more than enough to recover for Bell Aircraft Corporation the total amount of the expenditures of $3,422,870.23 referred to above, and were so treated on the books of Bell Aircraft Corporation.

b. That it appears that in 1943 as a result of conference with the Internal Revenue Department, Bell Aircraft Corporation revised its formal method of amortizing the said costs of $3,422,870.23 against fixed price production contracts only and spread the amount of such costs over all of its fixed price and CPFF contracts for airplanes which Bell claims benefitted from the development work which it did. As a result, the amount of $3,422,870.23, adjusted to $3,374,465.00 by the elimination of certain overhead items was charged by Bell in 1943 against fixed price contracts and cost-plus-a-fixed-fee contracts as follows:

(1) Against fixed price contracts.....	$1,087,645.05
(2) Against CPFF contracts.....	2,286,819.95
Totals	$3,374,465.00

c. That Bell Aircraft Corporation has already been reimbursed by the Government under its CPFF contracts for $1,299,855.92 of the amount of $2,286,819.95 noted above and that the General Accounting Office, by informal exceptions No. 777, 778, and 779, has raised the question of whether such amounts were properly reimbursed to Bell. It also appears that Bell Aircraft Corporation has submitted, or is proposing to submit, claims for reimbursement under its CPFF contracts for the balance of the sum of $2,286,819.95.

The amount of $1,299,855.92 was subsequently recouped by the Government by a deduction from audit vouchers.

d. By letter dated 30 October 1944, subject "Amortization of Development Expenses on CPFF Contracts" directed to the Bell Aircraft Corporation Contracting Officer, Bell states that it did not include in its quotations on fixed price production contracts referred to in paragraph 1a. over which it originally amortized the development costs of $3,422,-870.23, the entire amount of such expenditures, but Bell does not indicate how much of such expenditures were, in fact, included in its fixed price quotations, and has failed to furnish any information which indicates that, notwithtstanding the views of the Resident Auditor and the Contracting Officer, it did not, in fact, recover through the fixed price production contracts referred to in paragraph 1a., the entire amount of such development expenses.

e. It appears that the said sum of $2,286,819.95 which Bell has charged on its books against CPFF contracts does not, in fact represent costs of performing such CPFF contracts and that reimbursement for such costs under the said CPFF contracts would result in Bell's receiving double payment from the Government therefor.

2. It is, therefore, the decision of the Contracting Officer that Bell is not entitled to reimbursement under its CPFF contracts for P-39 and P-63 airplanes for any portion of the said sum of $2,286,819.95.

/s/ H. B. Davies
H. B. DAVIES
Captain, Air Corps
Contracting Officer.

End

Per Curiam Decisions.

No. 13. UNITED STATES *v.* BELL AIRCRAFT CORP. Certiorari, 343 U. S. 913, to the Court of Claims. Argued October 16, 1952. Decided October 27, 1952. *Per Curiam:* The judgment is affirmed by an equally divided Court. MR. JUSTICE JACKSON took no part in the consideration or decision of this case. *Paul A. Sweeney* argued the cause for the United States. With him on the brief were *Acting Solicitor General Stern, Assistant Attorney General Baldridge* and *Morton Hollander. Howard C.*

Westwood argued the cause for respondent. With him on the brief were *Ansley W. Sawyer* and *W. Crosby Roper, Jr.* *John Lord O'Brian* was also of counsel for respondent. Reported below: 120 Ct. Cl. 398, 100 F. Supp. 661.